TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1940

No. 479

NORMAN J. PFAFF AND FRANK B. WALLACE, EXECUTORS OF THE ESTATE OF WILLIAM L. WALLACE, DECEASED, PETITIONERS,

vs.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED OCTOBER 1, 1940.

CERTIORARI GRANTED NOVEMBER 12, 1940.

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INDEX.

JUDD & DETWEILER (INC.), PRINTERS, WASHINGTON, D. C., DECEMBER 12, 1940.
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[fol. 1]

IN UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT

Docket No. 337

NORMAN J. PFAFF and FRANK B. WALLACE, Executors of Estate of William L. Wallace, Dec'd, Appellants,

vs.

COMMISSIONER OF INTERNAL REVENUE, Appellee

STATEMENT UNDER RULE 13

On Aug. 30, 1937, the Commissioner of Internal Revenue assessed a deficiency income tax for the taxable year ending Dec. 31, 1935, against Norman J. Pfaff and Frank B. Wallace as Executors of Estate of William L. Wallace for $637.02. On Nov. 29, 1937, said Executors filed their petition for a review by the Board of Tax Appeals. On Jan. 14, 1938, the Commissioner of Internal Revenue answered.

On June 20, 1939, a hearing was had before Hon. J. Russell Leech and on Sept. 30, 1939, he rendered his memorandum opinion. On the same day decision was entered.

On Dec. 28, 1939, said Executors duly filed their petition for review by this Court, together with their assignment of errors.

Hon. J. P. Wenchel appeared as counsel for appellee before the Board of Tax Appeals, and Samuel O. Clark, Jr., appears for Appellee on this appeal.

Laurence Sovik appears for appellants, and except as above there has been no change in the parties or their attorneys.

[fol. 2] BEFORE UNITED STATES BOARD OF TAX APPEALS

DOCKET ENTRIES

APPEARANCES:

For Petitioners: Laurence Sovik, Esq.
For Respondents: S. U. Hiken, Esq.

1937
Nov. 29—Petition received and filed. Taxpayer notified. (Fee paid.)

DOCKET ENTRIES—Continued

1937
Nov. 29—Copy of petition served on General Counsel.

1938
Jan. 14—Answer filed by General Counsel.
Jan. 14—Request for circuit hearing in New York City filed by General Counsel.
Jan. 18—Notice issued placing proceeding on New York City Calendar. Copy of answer and motion served on taxpayer.

1939
Apr. 20—Hearing set June 19, 1939, Buffalo, New York.
June 20—Hearing had before Mr. Leech on merits. Submitted. Appearance of Laurence Sovik, Esq., filed. Petitioner's brief due 7/15/39. Respondent's brief due 8/12/39. Reply due 8/26/39.
July 8—Transcript of hearing of June 20, 1939, filed.
July 24—Motion for leave to file brief filed by taxpayer—brief lodged. 7/25/39 granted.
Aug. 11—Brief filed by General Counsel.
Sept. 30—Memorandum opinion rendered—Mr. Leech, Division 6. Decision will be entered for the respondent.
Sept. 30—Decision entered—J. Russell Leech, Division 6.
[fol. 3] Dec. 28—Petition for review by U. S. Circuit Court of Appeals, Second Circuit, with assignment of error filed by taxpayers.
Dec. 28—Proof of service filed by taxpayer.

1940
Feb. 9—Agreed praecipe for record filed with proof of service thereon.

BEFORE UNITED STATES BOARD OF TAX APPEALS

PETITION

The above named petitioners hereby petition for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency IT: A:1, JBW:90D, dated August 30, 1937, and as a basis of their proceeding allege as follows:

1. Petitioners are the executors of the estate of William L. Wallace, deceased. Norman J. Pfaff, one of said executors, resides at 555 Harvard Street, Rochester, N. Y., and Frank B. Wallace, one of said executors, resides at 1134 West Culver Street, Phoenix, Arizona. The variance between the notice of deficiency and the title herein is due to the omission of the name of Frank B. Wallace as one of the executors of said estate.

2. The notice of deficiency, a copy of which is hereto attached and marked Exhibit "A", was mailed to petitioners on August 30, 1937.

3. The tax- in controversy are income taxes for the fiscal year ended December 31, 1935, and the deficiency tax claimed is in the amount of $637.02, all of which amount is in dispute.

4. The determination of the tax set forth in the said notice of deficiency is based upon the following error:

[fol. 4] The inclusion in income for the year 1935 of $5,689.19 in outstanding accounts receivable of the partnerships in which taxpayer was a member prior to his death on December 25, 1935.

5. The facts upon which petitioners rely as the basis of this proceeding are as follows:

(a) At the time of his death taxpayer had an interest in an undeterminable quantity of accounts receivable of two partnerships. Taxpayer was a member of the partnership known as Wallace, Brust, Muench & Potter under an agreement dated July 1, 1934, said partnership to terminate June 30, 1935. Taxpayer was also a member of the partnership known as Wallace, Brust, Muench, Potter & Spire under an agreement dated July 1, 1935, said partnership to terminate June 30, 1936.

(b) Taxpayer died December 25, 1935.

(c) During the year 1936 and up until Oct. 1 of that year, the executors of the estate of said taxpayer received from said partnership the sum of $5,189.19, which sum represented the difference between taxpayer's interest in the actual cash collections of said accounts receivable of $6,193.14 and his share in the expense of collecting, amounting to $1,003.95.

On Oct. 1, 1936, taxpayer's interest in the remaining accounts was sold by the executors of his estate under an order of Surrogate's Court of Onondaga County, and the price obtained at such sale and received by the executors was $500.00.

(d) The amount received by the estate of said taxpayer from said accounts receivable totaled $5,689.19, all of said moneys being received during the year 1936.

(e) The books of account of both the aforesaid partnerships are kept on a cash basis.

[fol. 5] (f) Under both partnership agreements it was understood and agreed that at the end of each month during the existence of said partnerships there should be an accounting for the preceding month and, after the deduction of expense of said partnership, there should be paid to each partner the proportionate share of profits in said partnership.

(g) Under the terms of said partnership agreements, the amounts allocated to the account of each partner were determined upon the proceeds actually received in cash from the patients' accounts receivable and each partner was merely entitled to his share of the proceeds of the patients' accounts actually collected.

(h) In accordance with said partnership agreements, there was payable to taxpayer for December, 1935, the sum of $163.96.

Wherefore, petitioners pray that this Board may hear the proceeding and disallow the deficiency tax as claimed.

Laurence Sovik, Attorney-in-Fact, 930 University Block, Syracuse, New York.

(Verifications.)

EXHIBIT "A" TO PETITION

Aug. 30, 1937.

Norman J. Pfaff, Executor, Estate of William L. Wallace, Deceased, 810 South Crouse Avenue, Syracuse, New York.

SIR:

You are advised that the determination of the income tax [fol. 6] liability of William L. Wallace, deceased, for the

taxable year ended December 31, 1935, discloses a deficiency of $637.02, as shown in the statement attached.

In accordance with section 272(a) of the Revenue Act of 1934, notice is hereby given of the deficiency mentioned. Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C1:P:7. The signing and filing of this form will expedite the closing of your return by permitting an early assessment of the deficiency and will prevent the accumulation of interest, since the interest period terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully, Guy T. Helvering, Commissioner, by
(Signed) Chas. T. Russell, Deputy Commissioner.

STATEMENT

IT:A:1
JBW:90D

In re: Norman J. Pfaff, executor, estate of William L. Wallace, deceased, 810 South Crouse Avenue, Syracuse, New York.

[fol. 7] Tax Liability for Taxable Year Ended December 31, 1935

	Liability	Assessed	Deficiency
Income tax	$1,445.90	$808.88	$637.02

The deficiency shown herein is based upon the report dated February 23, 1937, prepared by Revenue Agent Thomas J. Collins, a copy of which was transmitted to you. The report has been approved as submitted.

Careful consideration has been given to your protests dated April 19, 1937, and July 7, 1937, in connection with the report of the internal revenue agent in charge, and the

information submitted at a conference held in the office of that official, and in this office under date of July 28, 1937.

The adjustments made and computation of tax follow:

Net income shown on the return		$12,774.56
1. Partnership income increased	$5,689.19	
2. Foreign dividends received	427.50	6,116.69
		$18,891.25
Deduct:		
3. Domestic dividends decreased	$292.00	
4. Interest paid	243.21	
5. Taxes paid	653.16	1,188.37
Net income adjusted		$17,702.88

Explanation of Changes

1. Net amount of accounts receivable for services rendered by law partnership (accrued at the date of death) is included in taxable income in accordance with article 42(1) of Regulations 86, which provides that all accrued income, not applicable to a prior period, at date of death must be included in decedent's taxable income. See also the decisions of the United States Board of Tax Appeals [fol. 8] in the cases of Maurice L. Goldman et al., 15 Board of Tax Appeals, page 1341, and Clarence B. Davidson, executor, 20 Board of Tax Appeals 856, affirmed by Circuit Court of Appeals (2d) Ct. 43 Fed. (2d) 1077 A. F. T. R. 1025, wherein it was held that the income of the partnership, allowable to the deceased partner to the date of his death, should be included in the income tax return filed on his behalf for the period ended with his death, no distinction to be drawn between cases where the partnership or deceased partner was on a cash or accrual basis.

2. Amount is determined as follows: $380.00 transferred from item 10(a) on face of return plus $47.50 from Dome Mines stock, declared prior to date of death but paid on January 15, 1936.

3. Amount is determined as follows:

Transferred to foreign dividends (other income)		$380.00
Added:		
Declared prior to date of death, but paid subsequent thereto, included in accordance with the provisions of article 42-1 of Regulations 86:		
National Cash Register paid January 15, 1936	$25.00	
Easy Washing Machine paid December 31, 1935	37.50	
Phillip Morris & Co. paid December 31, 1935	25.00	
North American Co. paid January 1, 1936	.50	88.00
Net decrease		$292.00

[fol. 9] 4 and 5. Accrued interest and accrued taxes at date of death are allowed as deductions in accordance with the provisions of article 42-1 of Regulations 86.

Computation of Tax

Total net income adjusted		$17,702.88
Less:		
Personal exemption		1,000.00
Income subject to surtax		$16,702.88
Less:		
Dividends	$582.50	
Earned income credit 10% of $14,000.00	1,400.00	1,982.50
Net income subject to normal tax		$14,720.38
Normal tax at 4% on $14,720.38		588.82
Surtax on $16,702.88		857.32
Total		$1,446.14
Less:		
Tax paid at source	$.24	.24
Total amount assessable		$1,445.90
Tax previously assessed; account No. 805610		808.88
Deficiency in tax		$637.02

A copy of this letter, together with a copy of the statement, has been mailed to your representative, Mr. Laurence Sovik, in accordance with the authority contained in the power of attorney executed by you and on file with the Bureau.

[fol. 10] BEFORE UNITED STATES BOARD OF TAX APPEALS

ANSWER

Now comes the respondent by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition of the above-named taxpayers, admits and denies as follows:

1. Admits the allegations in paragraph 1.

2. Admits the allegations in paragraph 2.

3. Admits the matter contained in paragraph 3, except it is denied that the taxes in controversy are for the fiscal year.

4. Denies the errors complained of in paragraph 4.

5. (a) Admits the matter set forth in paragraph 5 (a), except it is denied that the quantity of accounts receivable of the two partnerships was undeterminable.

(b) Admits the matter set forth in paragraph 5 (b).

(c) Admits the matter set forth in paragraph 5 (c).

(d) Admits the matter set forth in paragraph 5 (d).

(e) Admits the matter set forth in paragraph 5 (e).

(f) Denies the matter set forth in paragraph 5 (f).

(g) Denies the matter set forth in paragraph 5 (g).

(h) Denies the matter set forth in paragraph 5 (h).

6. Denies generally and specifically each and every allegation contained in taxpayers' petition, not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that taxpayers' appeal be denied.

J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue.

[fol. 11] BEFORE UNITED STATES BOARD OF TAX APPEALS

MEMORANDUM OPINION

LEECH:

Respondent determined a deficiency of $637.02 in income tax of petitioners' decedent for the period January 1, 1935, to the date of his death on December 25, 1935. This deficiency arises through the inclusion of the sum of $5,689.19 in decedent's gross income for that period, under section 42 of the Revenue Act of 1934. This sum was so treated on the ground that it represented the amount accrued to decedent at the date of his death with respect to his interest in certain accounts receivable due two partnerships of which decedent had been a member and covering services rendered by them during his lifetime.

The decedent was a practicing physician. During 1935 he was a member of two medical partnerships, one created in 1933 and dissolved by limitation of the partnership agreement on June 30, 1935, and the other created on July 1, 1935, and in existence at the date of his death on December 25 of that year. Each of these partnerships maintained its accounts on a cash basis. In each partnership the decedent was entitled to 40 per cent of the profits. The second partnership, upon organization, took over the assets and assumed the liabilities of the prior partnership.

At the time of decedent's death there were partnership accounts outstanding in a total amount of $69,061.59 for services rendered patients during decedent's lifetime. How much of this total represented accounts receivable of the first partnership is not disclosed. Between the date of decedent's death and October 1, 1936, net payments received on these accounts aggregated $16,251.21, of which [fol. 12] $5,961.80 was paid decedent's estate as his net distributive share. On the last named date decedent's interest in the remaining uncollected accounts was sold by his executors for $500. In the estate tax return filed for decedent's estate his interest in these uncollected accounts of the partnership, as of the date of his death, was included at a value of $6,693.14.

In determining the disputed deficiency, respondent increased decedent's gross income by $5,689.19, as the sum accruable on account of his interest in these partnership receivables at the time of his death, under section 42 of the

Revenue Act of 1934. How this amount was arrived at is not disclosed.

Petitioners contend that there was no amount accruable to their decedent at the time of his death with respect to partnership receivables because the partnerships in question maintained their accounts on a cash basis and, consequently, realized no income until the actual collection of the accounts. The argument then follows that decedent, as a member of the partnerships, accordingly cannot be held to have become entitled to any payment from the partnerships until these accounts were actually collected. It is then urged that, since there was no obligation due decedent at his death, no amount could be considered as then accrued to him.

We think this reasoning overlooks the fact that one of these partnerships had terminated on June 30, 1935, prior to decedent's death, and thus within the taxable period here in question. With respect to the accounts due this partnership at the time of its dissolution, we think there could be no question that decedent's 40 per cent interest therein was distributable thereupon to him and that the asset value of such interest was a proper item of accrual had decedent maintained his accounts on an accrual basis. The effect of [fol. 13] section 42, cited supra, was to place decedent on that basis for the period during which that interest became distributable. See Lillian O. Fehrman, Exrx., 38 B. T. A. 37. The second partnership was organized on July 1, 1935. It received from the several partners their interests in the assets of the first partnership and assumed their liabilities in connection therewith. The second partnership also stood dissolved upon decedent's death. Its assets, including the accounts receivable here in dispute, were then distributable to the several partners. Any gain represented thereby was includable in income of a deceased partner, irrespective of the fact that the partnership maintained its accounts upon the cash basis. Guaranty Trust Company of New York v. Commissioner, 303 U. S. 493; cf. Bull v. United States, 295 U. S. 247.

Since the partnership was dissolved by decedent's death, we think his right then accrued to the distributive share of the partnership assets, consisting of the accounts receivable, and that the amount then reasonably determinable as collectible constituted income accrued as of date. In this connection it is noted that respondent, in his determination

of the deficiency, has not included in decedent's income, as accrued, his 40 per cent share in these accruables, at their face amount. Only approximately 20 per cent of that face value is included. The burden is upon petitioners to establish error. There is no evidence that respondent's determination as to the amount which could reasonably be anticipated as collectible as of the date of decedent's death is incorrect or excessive. In fact, the only evidence bearing upon the accuracy of such estimate tends to sustain its reasonableness. The amount included by respondent is less than the amount actually realized from decedent's interest in these receivables and is less than the amount declared [fol. 14] by petitioners as the value of these receivables in the estate tax return which they filed.

Petitioners contend that the question here involved is controlled by our decision in Lillian O. Fehrman, Exrx., supra, but the facts in that case were quite different from those presented here. There the income sought to be included by the respondent was a net percentage of net profits of a business, due under the contract of employment of decedent, at the conclusion of the taxable year in which the death of the decedent occurred. These profits for the year, and the portion to which the decedent was entitled, could only be computed as of the close of that year. In that case the petitioner's decedent's death gave rise to no right in his estate to payment of any amount. Such right accrued only at the termination of the year in which petitioner's decedent died and then only as to such profits as might be realized upon the business of that entire year.

The respondent's determination is affirmed.

Enter.

Decision will be entered for the respondent.

BEFORE UNITED STATES BOARD OF TAX APPEALS

DECISION

Pursuant to the determination of the Board, as set forth in its memorandum opinion entered September 30, 1939, it is

Ordered and Decided: That there is a deficiency in income tax for the period January 1, 1935, to December 25, 1935, in the amount of $637.02.

Enter.

(Signed) J. Russell Leech, Member.

[fol. 15] IN UNITED STATES CIRCUIT COURT OF APPEALS

PETITION FOR REVIEW OF BOARD DECISION

Taxpayers, petitioners in this cause, by Laurence Sovik, counsel, hereby file their petition for review by the Circuit Court of Appeals for the Second Circuit of a decision by the United States Board of Tax Appeals rendered on September 30, 1939, determining a deficiency in petitioners' Federal income tax for the period January 1, 1935 to December 25, 1935, and respectfully shows:

I

Petitioners are executors of the estate of Dr. William L. Wallace, who died on Dec. 25, 1935. Dr. Wallace was a member of a partnership of practicing physicians and surgeons and reported his income on a cash basis based on the calendar year. The partnership likewise kept its books and records on a cash basis.

This case involves two partnership agreements, because in the taxable year in which Dr. Wallace died the partnership agreement of July 1, 1933 (petitioners' Exhibit 1) expired on June 30, 1935. At that time a new partner was taken in and a new partnership agreement executed (petitioners' Exhibit 2), which was to continue until June 30, 1936, but was terminated by the death of Dr. Wallace on December 25, 1935.

Each of these partnership agreements provides in paragraph eighth thereof that at the end of each month there shall be an accounting for the preceding month of—"all partnership gains and losses and there shall be paid to each of said partners, after the deduction of the expenses of said partnership, the proportionate share of the profits of said co-partnership as hereinbefore specified."

[fol. 16] The evidence discloses that the partnership accounts were kept on a cash basis and no entries were made on the books until the money for the particular service had been received by the partnership. In addition to the books of the partnership the partnership maintained a card system by which the name of each patient was listed on a separate card. As services were rendered to each patient, whether the case was then completed or not, an entry was made on the card showing the work which was done at a

particular time. Although sometimes charges for particular visits were entered on the card, ordinarily no bill was sent out for the services until the case had been completed. In many cases no charge was ever made and no bill ever sent and, in other cases, upon the completion of the case the individual charges which appeared on the card, if any, might be ignored and the doctor in charge of the case would make a flat charge for the entire case, at which time a bill would be sent out.

At the date of Dr. Wallace's death it was impossible to ascertain what accounts receivable had accrued to the partnership because some of the cases were charity cases and others were unfinished. The amount of the accounts receivable of the partnership on that particular date was indeterminate and was reduced to a determinate amount only after all of the cases then under treatment had been completed and charges made against them.

The books of the partnership showed only the expenditures actually made and the cash actually received. The monthly accountings which were had pursuant to the eighth paragraph of each of the partnership agreements were only with reference to the matters appearing on the books. With reference to the matters appearing on the card system, no [fol. 17] part of the monies which would be received from such services could be said to have accrued to any particular partner because charges would have to be made, expenses of the partnership deducted and bills rendered before any monies accrued or became distributable to any individual partner.

On the death of Dr. Wallace, Dec. 25, 1935, the cases contained on the card system were estimated to have a value of $69,601.13. After these accounts had been collected, so far as possible, the surviving partners rendered an accounting and paid over to petitioners the sum of $5,189.19, which payments were made during the calendar year of 1936. On Oct. 2, 1936, Dr. Wallace's interest in the remaining accounts was sold at public auction, pursuant to an order of the Surrogate's Court of Onondaga County, New York, and the price obtained at such sale by petitioners was $500.00. Thus the total received by petitioners from the partnership in the calendar year of 1936 totaled $5,689.19. None of this amount was included in petitioners' return for the calendar year of 1935. The Commissioner assessed a deficiency tax in the sum of $637.02 upon the ground that the sum received

in 1936 was accrued to Dr. Wallace at the time of his death in 1935.

II

Assignments of Error

Petitioners assign as error the following acts and omissions of the Board of Tax Appeals:

(1) The amount received for said accounts receivable was not taxable income for the year 1935.

(2) The amount received for said accounts receivable was not income accrued to Dr. Wallace at the time of his death.

(3) Said income did not accrue until the year 1936, when it was actually received.

[fol. 18] (4) The amount collected from said accounts receivable in the year 1936 was not accounts receivable at the time of Dr. Wallace's death.

(5) There was nothing on the books of the partnership accrued to Dr. Wallace at the time of his death.

(6) At the time of his death Dr. Wallace had no right, title or interest in and to said accounts receivable, except as provided in said partnership agreements.

(7) There was no income accrued up to the date of Dr. Wallace's death within the meaning of section 42 of the Revenue Act of 1934.

(8) The Court erred in holding that said accounts receivable were distributable to the several partners at the date of Dr. Wallace's death.

(9) The Court erred in holding that the amount reasonably determinable as collectible at the time of Dr. Wallace's death constituted income accrued as of that date.

(10) The Court erred in holding that it was necessary for petitioners to establish the amount which could reasonably be anticipated as collectible as of the date of Dr. Wallace's death.

Laurence Sovik, Counsel for Petitioners, 930 University Block, Syracuse, New York.

(Verifications.)

[fol. 19] IN UNITED STATES CIRCUIT COURT OF APPEALS

NOTICE OF FILING PETITION FOR REVIEW

Please take notice that petitioners on the 28th day of December, 1939, filed with the Clerk of the United States Board of Tax Appeals at Washington, D. C., a petition for review by the Circuit Court of Appeals for the Second Circuit of the decision of the Board of Tax Appeals heretofore rendered in the above entitled cause. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you. Dated at Syracuse, N. Y., this 23rd day of December, 1939.

Respectfully, Laurence Sovik, Counsel for Petitioners, 930 University Block, Syracuse, N. Y.

Personal service of the foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein is hereby acknowledged this 28th day of December, 1939.

J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

[fol. 20] BEFORE UNITED STATES BOARD OF TAX APPEALS

PRAECIPE FOR TRANSCRIPT OF RECORD

To the United States Board of Tax Appeals:

You are hereby requested to prepare, certify and transmit to the Clerk of the United States Circuit Court of Appeals for the Second Circuit, with reference to the petition for review heretofore filed by petitioners in the above entitled matter, a transcript of the record in the above cause prepared and transmitted as required by law and by the rules of said Court, and to include in said transcript of record the following documents, to wit:

1. Reporter's minutes of hearing on June 20, 1939, at Buffalo, N. Y., with Exhibits 1, 2, 3 and A4.
2. Pleadings before the Board of Tax Appeals as follows:

(a) Petition for redetermination.
(b) Answer of respondent.

3. Memorandum opinion of Board of Tax Appeals.

4. Decision of Board of Tax Appeals.
5. Petition for review filed by petitioners in the above cause, including assignments of error.
6. Notice of filing petition for review, together with admission of service thereof.
7. The docket entries of proceedings before the Board.
8. This praecipe.

Dated, February 6th, 1940.

Laurence Sovik, Counsel for Petitioners, Office and P. O. Address, 930 University Block, Syracuse, New York.

[fol. 21] Service of a copy of the within praecipe is hereby admitted this 9th day of February, 1940. Agreed to
J. P. Wenchel, Attorney for Respondent on Review.

BEFORE UNITED STATES BOARD OF TAX APPEALS

Statement of Evidence

EVIDENCE ON BEHALF OF PETITIONER

Thereupon, the petitioner, to maintain the averments of its petition, introduced the following proof:

DOROTHY PELLENZ, called as a witness by and on behalf of the petitioner, having been first duly sworn, was examined and testified as follows:

The Clerk: Dorothy Pellenz.

Mr. Sovik: Your Honor, these are original documents. May I have it appear that copies may be later substituted for the originals?

The Member: The Board will order now that photostatic copies may be substituted for any original exhibits received in evidence in this case.

Mr. Sovik: Thank you.

The Member: Or ordinary copies, subject to check by the opposing party.

Direct examination.

By Mr. Sovik:

Q. Miss Pellenz, you are a resident of Syracuse, New York?

A. Yes.

[fol. 22] Q. And in his lifetime you were acquainted with Dr. Wallace?

A. I was.

Q. Who has been mentioned here?

A. Yes.

Q. I show you Exhibit 1 marked for identification and ask you whether or not that is your signature?

A. Yes.

Q. And at that time you were a Notary Public of the County of Onondaga?

A. Yes.

Mr. Sovik: Offer Exhibit 1 in evidence as being a partnership agreement existing between the decedent and the other parties mentioned in Exhibit Number 1. Under our rules of evidence, it would be admissible without proof in view of the fact that it was acknowledged, but I am not sure whether that is the rule in this court or not.

Mr. Hiken: May I just ask a question about that? Was this document signed by the persons whose signatures appear thereon at the time you took the acknowledgement?

The Witness: Yes.

Mr. Hiken: And you saw them sign it?

The Witness: Yes.

Mr. Hiken: And this is the original document that was signed in your presence?

The Witness: Yes.

Mr. Hiken: No objection.

The Member: Received in evidence as petitioner's Exhibit Number 1.

The said document (agreement so offered and received in evidence) was marked petitioner's Exhibit 1, and made a part of this record.

By Mr. Sovik:

Q. I show you petitioner's Exhibit 2 marked for identification, Miss Pellenz, and ask you whether or not that is your signature?

A. Yes.

[fol. 23] Q. Appearing on the last page?

A. Yes.

Q. And at that time were you a Notary Public for the County of Onondaga?

A. Yes.

Q. Do you know the signatures on the next to the last page of this exhibit, William L. Wallace, Herbert O. Brust, Carl Muench, Carlton F. Potter, A. J. Spire?

A. Yes.

Q. Did you see those men sign this exhibit?

A. Yes.

Mr. Sovik: I offer it in evidence as partnership agreement existing between the men just mentioned.

Mr. Hiken: You saw these gentlemen sign this document on the date appearing in the acknowledgment?

The Witness: Yes.

Mr. Hiken: And they signed in your presence at that time, is that correct?

The Witness: That is correct.

Mr. Hiken: No objection.

The Member: Received as petitioner's Exhibit Number 2.

The said document (partnership agreement) so offered and received in evidence was marked petitioner's Exhibit 2, and made a part of this record.

By Mr. Sovik:

Q. Now, Miss Pellenz, you were employed by the gentlemen that are mentioned in Exhibits 1 and 2?

A. Yes.

Q. And you also were employed by Dr. Wallace for a number of years?

A. Yes.

Q. How many years?

A. Twenty-two.

Q. Among your other duties you were the bookkeeper?

A. Yes.

Q. Were you, beginning July 1, 1935, the bookkeeper for the partners mentioned in Exhibit Number 2?

A. Yes.

[fol. 24] Q. And were you the bookkeeper for the partners named in Exhibit Number 1 between July 1, 1933, and July 1, 1935?

A. Yes.

Q. And you were the bookkeeper for the partners mentioned in Exhibit 2 up until the time that Dr. Wallace died on December 25, 1935?

A. Yes.

Q. And you also were the bookkeeper for the estate of Dr. Wallace?

A. Yes.

Q. And were you also the bookkeeper for the remaining partners under Exhibit 2 after Dr. Wallace died and until the affairs of that partnership were wound up?

Mr. Hiken: May it please Your Honor——

A. Yes, I was.

Mr. Hiken: —all of these questions have been leading. They have been stating the answer in the form of the question. I suggest that counsel be instructed to refrain from leading the witness. I haven't objected heretofore because it has not been too important.

Mr. Sovik: Your Honor, may I say this——

The Member: They have been up to this point. Proceed.

Mr. Sovik: I was asking in that form only for the purpose of simplifying the situation.

The Member: Proceed.

By Mr. Sovik:

Q. Now, Miss Pellenz, will you tell us briefly what books you kept for these partners under Exhibit Number 2?

A. Well, I have, of course, a book of account of all their receipts and expenses and the distribution to the various partners.

Q. Was there anyone else that kept any books or records——?

A. No.

Q. —for these partners?

A. No.

[fol. 25] Q. Were all of the receipts from July 1, 1935, to the time of Dr. Wallace's death handled by you as the bookkeeper for these partners?

A. Yes.

Q. And were all of the receipts beginning July 1, 1933, to July 1, 1935, handled by you as the bookkeeper for the partners mentioned in Exhibit Number 1?

A. Yes.

Q. Now then, what did you do with the receipts that you handled you have testified?

A. Well, they were all deposited in the bank and I paid the expenses and made an accounting to the partners at the

end of each month. I gave them a check for whatever—well, I usually decided what distribution would be made, depending on the balances on hand.

Q. And the money was deposited in what bank?

A. Oh, that last partnership, with the Syracuse Trust Company, and the other one, I think, was in the Merchants National Bank. There are two banks.

Q. Was all of the money disbursed by you by check or was some disbursed in cash?

A. By check only.

Q. By check only. Did you draw these checks?

A. Yes.

Q. And the checks were signed by—who signed the checks?

A. The checks might be signed by any one of the partners, although I also had power of attorney, whichever one happened to be convenient, usually Dr. Wallace when he was alive, because he happened to be the most convenient person.

Q. Were there any entries kept on any of these books by you which at any time allotted to any person, any one of these men——.

Mr. Hiken: I object. The books speak for themselves and constitute the best evidence.

The Member: I think the books would speak for themselves. This witness who kept the books and made, as she said, all the entries in those books—am I correct?

[fol. 26] The Witness: That is correct.

The Member: If she has any personal recollection on this aside from any written record, then she can state what that personal recollection is. Do you have a personal recollection aside from what the books show as to whether or not any such entry was made on the books?

The Witness: Yes, I remember very well.

The Member: Well, what is the answer.

The Witness: No, there never were any such.

The Member: Objection overruled. Exception noted for the respondent.

By Mr. Sovik:

Q. Now, you also kept track of the accounts receivable among your duties as bookkeeper?

A. Yes.

Q. And you sent out bills to the various patients and accounts?

A. Yes.

Q. And you handled collections of those accounts yourself?

A. Yes.

The Member: Don't you think the question would be better put if it were "do you"?

Mr. Sovik: Yes. Thank you.

By Mr. Sovik:

Q. Now, Miss Pellenz, do you know the amount of cash on hand or on deposit of the partnership mentioned in Exhibit Number 2 as of the time of Dr. Wallace's death, that is December 25, 1935?

Mr. Hiken: I object, if it please Your Honor. There is no issue in the case of the cash on hand at the time of the decedent's death.

Mr. Sovik: Well, if counsel will concede that amount, that is satisfactory indeed.

The Member: Then the question is withdrawn?

[fol. 27] Mr. Sovik: I will withdraw the question if counsel will concede for the record there was approximately $150 odd of cash on hand on the date of this decedent's death, December 25, 1935, in the partnership funds.

Mr. Hiken: I am not conceding any amount. I couldn't do that, Your Honor. My point is that it is immaterial what cash was on hand.

The Member: We do not see its relevancy either, but for the purpose of the record the objection is overruled, and an exception is granted to the respondent.

Mr. Sovik: You may answer.

A. The cash was $138.58.

Mr. Sovik: Would you like to see that, counsel, in the books?

Mr. Hiken: No. That is all right. I just wanted to see what she was reading from.

The Member: The witness is testifying from a book which she herself kept.

The Witness: That is right.

Mr. Sovik: She has testified as to that question.

The Member: Very well.

By Mr. Sovik:

Q. Now, Miss Pellenz, in the course of your duties as a bookkeeper, you became familiar with these accounts which appear on the books?

A. Yes, sir.

Q. And will you state whether or not as of December 25, 1935, all of those accounts were for services rendered up to the time of the death of Dr. Wallace?

A. Yes.

Q. And were some of those accounts for services which had not been completely finished?

A. Yes, a good many would have been.

[fol. 28] Q. Now, have you any information or any books or records from which you could distinguish which of these accounts which were on the books as of December 25, 1935, were for services which were completed or services which were incompleted?

Mr. Hiken: I object, if it please Your Honor. I cannot see where it is material whether or not services for which bills had been sent out had been completed or not. The mere fact that the bills were outstanding would indicate that they were owing to the partnership firm that had rendered them.

Mr. Sovik: I perhaps should ask one more preliminary question and qualify that. Now, Miss Pellenz——

Mr. Hiken: Just a minute. I request that the objection be ruled upon in the present form of the record.

The Member: Well, the Board refuses to pass on it until the question is asked. You will get your ruling.

Mr. Sovik: Thank you, Your Honor.

By Mr. Sovik:

Q. Were all of the accounts on the books of the partnership on December 25, 1935, accounts for which statements had previously been rendered?

A. No.

Q. In other words, there were a number of accounts on the books which we will say any one of these partners, or certain of these partners, where they had not completed the services which they were performing for these particular patients, is that right?

A. That is right.

Q. And there came a time when those services were completed?

A. Yes.

Q. And when those services were completed the account was made up by the respective partner who had charge of that particular patient?

A. That is right.

[fol. 29] The Member: Now just a minute, to get back to the question to which the objection was made. Will you please read that question? As we recall the objection was on the basis of relevancy. Objection is overruled and exception is noted for the respondent.

By Mr. Sovik:

Q. Now, Miss Pellenz, you have testified that you were familiar with these accounts. Was there any way as of December 25, 1935, that you could have, as the bookkeeper for these partners, for distinguishing between unfinished business and finished business?

A. No.

Q. Now there did come a time, Miss Pellenz, when all of the services for these accounts which were on the books on December 25, 1935, were completed?

A. Yes.

Q. A figure was placed on each account?

A. Yes.

Q. Do you know what that figure ultimately was?

Mr. Hiken: May it please Your Honor, I object on the ground of relevancy.

The Member: The objection overruled. Exception is noted for the Respondent.

A. That figure totaled $69,601.59.

Q. Now, between the time that Dr. Wallace died and October 2, 1936, certain sums were collected on these accounts?

A. Yes.

Q. Now, do you know what that amount was, Miss Pellenz?

A. Yes.

Mr. Hiken: I object, if it please, Your Honor.

Q. Will you so state?

Mr. Hiken: I withdraw the objection on that question. Did you ask her to state?

Mr. Sovik: Yes.

[fol. 30] Mr. Hiken: I object, if Your Honor please. It is immaterial what collections were subsequently made on accounts accrued as of a particular date.

The Member: We understand your position. The objection is overruled and exception is noted for the respondent.

A. The amount was $16,251.21.

By Mr. Sovik:

Q. Now that sum was the amount which was collected in winding up the affairs of these partners under Exhibit Number 2?

A. It is under both.

Q. Under both Exhibits Number 1 and 2?

A. Yes, sir, a total.

Q. All right. And there came a time when the share to which Dr. Wallace, if he had been living, would have been entitled to, that was paid over to the executors of Dr. Wallace's estate?

A. Yes.

Q. Now can you tell me when that was?

A. Well——

Q. Was it from time to time?

A. That was paid monthly.

Q. Monthly?

A. From the time he died up to the final settlement.

Q. Were there any payments made in 1935?

A. Yes. In 1935 there was $163.93 payable.

Q. How much was paid in 1936?

A. In 1936 there was $5,961.80.

Q. Were there any other sums paid?

A. Yes, the money from the sale of the accounts.

Q. Now there came a time when Dr. Wallace's interest in the accounts under Exhibits Number 1 and 2 were sold?

A. Yes.

Q. They were sold at public auction?

A. Yes.

Q. When was that, if you know?

A. October 1, 1936.

Q. How much were they sold for?

A. Five hundred dollars.

[fol. 31] Q. Now, other than sums to which you have testified, did the executors of the Wallace estate receive any-

thing other than that for his interest in these accounts or in these partnership agreements, Exhibits Number 1 and 2?

A. No.

Mr. Sovik: I think that is all, Your Honor.

The Member: Cross-examine.

Cross-examination.

By Mr. Hiken:

Q. Didn't the estate of Dr. Wallace receive some distribution some time from the sale of some uncollected accounts?

A. Yes. Received a lump sum.

Q. Was that included in the sum of $5,961.80 that was received by the estate in 1936?

A. Well, that was received from the partnership before the accounts were sold, his share of the accounts was sold and there was a $500 lump sum final settlement to the estate.

The Member: Who sold those accounts?

The Witness: They were sold by the attorney for the estate, or through his office.

Mr. Sovik: That is, Dr. Wallace's interest was sold?

The Witness: Yes, Dr. Wallace's share was sold.

Mr. Sovik: I didn't want Your Honor to be confused. In other words, Your Honor, I want it to appear correctly on the record. All of these accounts were not sold, Miss Pellenz?

The Witness: No.

Mr. Sovik: Just Dr. Wallace's interest in those accounts in cleaning up the partnership affairs?

The Witness: Yes.

By Mr. Hiken:

Q. May I see the books from which you were reading a moment ago?

A. You can turn the book over to the year. There is 1935, for instance. Those are the monthly statements.

[fol. 32] Q. Do these books constitute all the books kept by you for the two partnerships described in Exhibits 1 and 2?

A. Yes.

Q. And these are the originals of the books kept?

A. They are.

Q. Will you show me where the accounts receivable that were owing to each of these partnerships appear in these books on December 25, 1935?

A. They don't appear on the books. The accounts receivable.

Q. You mean the firm kept and you, as bookeeper of the firm, kept no accounts receivable?

A. We had a card for every account, but we had no record on our books. They were entered on a cash basis.

Q. This book that you have here is only a cash basis, is that correct?

A. That is right.

Q. And it contains no information concerning the accounts receivable which all of the partnerships had on December 25, 1935, is that correct?

A. That is right.

Q. But you have card records which do show that?

A. Yes.

Q. Do you have those card records with you?

A. No, I haven't.

Q. What was the system of billing that you used in connection with your activities as bookkeeper for these two partnerships in 1935?

A. We had a card for each patient with the service listed on there with the charges which the Doctor gave us. When he had completed his charges, he gave us the statement and we sent the statements, and whenever they paid they were entered on the books, when they were paid.

Q. They were only entered on the books when they were paid?

A. Yes.

Q. But they were entered on the cards for each patient as bills were sent out?

A. Yes.

Q. And you say——

[fol. 33] The Member: Just a minute. We understand a little, we think, about what the witness is talking about, and we want it in the record. We think it is this, and if we are not right we want to be corrected, that there was maintained in that office a card for each patient of each doctor and member of that partnership, is that so?

The Witness: That is right.

The Member: And as services, as a call was made or an examination was made of a patient, no matter whether it was a completed case or not, the entry on that card was made showing the work which was done at that particular time for that particular patient, and a charge made on that card, is that right?

The Witness: The charge might not have been made until maybe some time later after it was completed, but the services were supposed to be entered after they were made.

The Member: But no bill was sent out for those services, that is, there was no charge made for them until the work for which that charge was made was completed, is that so?

The Witness: That is right.

The Member: That is to say, we think that that is the picture here, in most doctor's offices, and in some other offices, that a card system is maintained and that each patient has a card and on that card is put a reference or an item indicating what was done on that particular day, and a charge was entered there. We know of many, many doctors that do not send bills out more than once a year, and we don't know whether this was that picture, but this witness has certainly described to the Board Member sufficiently clearly for us to understand what their method of bookkeeping was.

The Witness: Frequently no charge was made at all. There might never be a charge made. It might be carried over.

[fol. 34] The Member: That is, you would not waste a two cent stamp on some of the patients, would you?

The Witness: That is right.

The Member: We think we understand the picture.

By Mr. Hiken:

Q. Let me ask you this, Miss Pellenz, when a particular card entry was made for a call made by one of the doctors, the nature of the services that he performed at that time were entered on the patient's card?

A. It was really his case record that I am referring to. He put down what the nature of his services were; then after the case was completed he would undoubtedly make a flat charge or something like that and we would send it out. The card contained both the account and the nature of the services.

Q. Well, on occasion, was an entry made at the time the service was performed for the particular charge that was made in connection with that same service, even though the case may not have been completed?

A. Sometimes.

Q. Do you have any information at this time as to the amount of bills rendered as of December 25, 1935, for both of these firms?

A. You mean they were mailed out?

Q. Actually outstanding. You have no information of any kind?

A. No, sir.

Q. Do you have any information of any kind showing the services rendered by either of these partnerships up to December, 1935, which remained unpaid at that date, whether or not they had been billed?

A. I have nothing as of December 25.

Q. You didn't bring those cards with you?

A. Well, there would be thousands of them, of course. It would be quite a——

Q. You stated a figure, $69,601.13, in your direct testimony?

A. Yes.

[fol. 35] Q. Exactly what does that figure represent?

A. Well, that figure represents an inventory of the accounts that were outstanding as of October 1, 1936. I do know that.

Q. As of October 31, 1936?

A. Yes, there are many that have been collected in the interval, so I worked backward to get the figure that was due approximately at the time of Dr. Wallace's death, the balance, the unpaid balance, the amount that had been paid.

The Member: Has the Government taxed this petitioner on his proportionate share of the accounts receivable by the partnership as of the date of the decedent's death?

Mr. Hiken: That is correct, Your Honor.

The Member: Accounts receivable?

Mr. Hiken: That is correct.

The Member: Without regard to their collectibility?

Mr. Hiken: No question was raised in that determination in connection with the collectibility of those accounts.

By Mr. Hiken:

Q. Now, as I understand it then, this figure of $69,601.13 represents the accounts receivable as estimated by you as of the date of Dr. Wallace's death, is that correct?

A. That is correct.

Q. And then Dr. Wallace's share, assuming that that entire amount had been collected, was endorsed by the partnership agreements referred to as Exhibits 1 and 2, is that correct?

A. Yes.

Mr. Hiken: No further questions.

The Member: Just a minute. When you say that Dr. Wallace's share of those accounts receivable—

The Witness: On October 1, 1936.

The Member: He died December 25, 1935?

[fol. 36] The Witness: That is right.

The Member: And when sold, they were sold at public auction?

The Witness: Yes.

The Member: And his interest was sold for $500, is that right?

The Witness: Yes.

The Member: That is all for the time being.

Mr. Hiken: Well, may I just repeat something for the purposes of the record.

By Mr. Hiken:

Q. The estate received five hundred dollars from the sale of some accounts receivable that were owing to the firm, is that correct?

Mr. Sovik: Your Honor, may I object to that question as highly improper in form and it might mislead the witness. In other words, it was not the accounts receivable that was sold but rather Dr. Wallace's interest in the partnership that was sold. I made that clear.

The Member: We just direct counsel to make his questions sufficiently clear to the witness, and the witness can answer it if she understands it, and if she doesn't understand it, she may say so.

Mr. Sovik: I think you and I both have the same idea in mind.

By Mr. Hiken:

Q. Miss Pellenz, in 1935 the partnership paid to the estate of Dr. Wallace an amount of $163.96, is that correct?

A. Yes.

Q. And then in 1936 these two partnerships paid to the estate of Dr. Wallace the amount of $5,961.80, is that correct?

A. That is correct.

[fol. 37] Q. And then also in 1936 the partnership, firms, paid to the estate of Dr. Wallace an additional $500, is that correct?

A. The partnership paid to Dr. Wallace?

Q. Who paid to Dr. Wallace?

A. That was from the sale of his share of the accounts. The partnership did not pay it to him.

Q. Some accounts receivable were sold in 1936, is that correct?

A. Yes.

Mr. Sovik: May I object to that question. This is a lay witness that does not understand the difference between the sale of a partnership interest and the sale of partnership accounts.

Mr. Hiken: Well, apparently——

Mr. Sovik: I will have to object to it, Your Honor, as improper in form and no foundation laid and not the best evidence. If you are going into that question. I have no objection to it appearing on the record what happened, and I believe it is admitted.

The Member: Just a minute. This is cross-examination, and the witness was asked a question on redirect examination about this sale. Now we want the witness to have all the opportunity in the world, and the witness is apparently an intelligent witness, to answer the question, but this is proper cross-examination. We overrule the objection and note an exception to the petitioner. You be very careful that you understand the questions as put and if you don't understand them, you can say so. If you do understand the questions, you may answer them.

The Witness: All right.

By Mr. Hiken:

Q. Miss Pellenz, that amount of $163.96, which was paid to the estate of Dr. Wallace in 1935, how was that amount [fol. 38] determined and from where was it received?

A. It was paid by the partnership, Dr. Wallace's distributive share of money he had taken in during 1935.

Q. How was that money taken in, was that money taken in from accounts on the card records of the partnerships that existed as of the date of Dr. Wallace's death?

A. Yes.

Q. And the amount of $5,961.80 that was paid to the estate of Dr. Wallace, what did that payment represent and from what source did that money come?

A. That was paid to his estate from the partnership accounts and represented his distributive share of money which they—cash which they had taken in from accounts that were due at the time of his death.

Q. That, just like the previous items, represents the distributive share of Dr. Wallace's on moneys due the two partnerships at the date of Dr. Wallace's death, is that correct?

A. Yes; money received after his death, of course.

Q. Money he received after his death but due at the time of his death?

A. Yes.

Q. Now, in addition to those two items, $500 was paid to the estate of Dr. Wallace as the result of the sale of Dr. Wallace's share in uncollectible accounts receivable which existed as of the date of his death when that share of his interest in those uncollected accounts receivable were sold at auction, is that correct?

A. Yes.

Q. You say that is correct?

A. Yes.

Mr. Sovik: Your Honor, I will object to it as improper in form, misleading the witness.

The Member: Objection overruled. Exception to the petitioner.

Mr. Hiken: That is all.

[fol. 39] Redirect examination.

By Mr. Sovik:

Q. You have been collecting accounts for Dr. Wallace and other doctors for a number of years?

A. Yes.

Q. And you have had considerable experience with accounts of doctors?

A. Yes.

Q. Now, how many years have you been collecting accounts receivable of doctors?

A. Twenty-two years.

Q. Now, in that period of time, what is your experience as to the collectibility of accounts, having in mind the time when the services had been performed and the time that the account is collected?

Mr. Hiken: I object.

Mr. Sovik: Qualifying.

The Member: You are testifying now as to the particular locality in which you were employed at that period and with particular reference to the clientele of this partnership, is that right?

A. Yes.

The Member: Objection overruled. Exception is granted to the respondent.

A. Do I understand you are asking the question according to the age of these accounts, how much they are worth?

By Mr. Sovik:

Q. That is right.

A. Well, the average account that is over six months old is purely a gamble, and up to that I should say—do you want that on a percentage basis?

Q. Well, what is your experience? We will say that the service has been performed and a bill is sent out. Now then, what is your experience as to the value of that account if the account is not paid within a specified period of time, and you tell us what that time is?

A. Well, within three months you might have a forty per cent chance of collecting the account if you have made a reasonable charge.

[fol. 40] Q. What is your experience after six months?

A. Well, after six months, I reduce it to about twenty per cent.

Q. What is your experience after eight months?

A. It would be reduced in proportion.

Q. Now, when counsel was examining you with reference to the accounts receivable, which were sold on October 2, 1936, will you state whether or not it was your information that this sale sold only the interest which Dr. Wallace had in those accounts?

Mr. Hiken: I object.

Mr. Sovik: Under Exhibits 1 and 2.

Mr. Hiken: I object, if it please Your Honor. Calling for a conclusion of the witness as to what was sold was Dr. Wallace's interest in the partnership. The witness has already testified that accounts receivable were sold.

The Member: Read the question.

(Whereupon the reporter read the question as recorded.)

The Member: Well, if it was only information that she had, she couldn't testify. It would be hearsay.

Mr. Sovik: I will ask her if she knows.

By Mr. Sovik:

Q. Do you know what interest was sold, Miss Pellenz, on October 1st or 2nd, whichever the case was, with reference to these accounts to which you have been testifying?

A. Well, I thought it was Dr. Wallace's share of the accounts.

Q. All right.

A. Only.

Mr. Sovik: Your Honor, I have here with me the actual bill of sale and I don't want to encumber the record unnecessarily. However, if it is of importance, Your Honor considers it of any importance——

The Member: We are not deciding what is or is not important. You will have to try your case.

[fol. 41] Mr. Hiken: Are you through with direct?

Mr. Sovik: No. I will just mark this exhibit.

By Mr. Sovik:

Q. Now, Miss Pellenz, after Dr. Wallace's death, is it a fact that certain of these accounts were turned over to various collection agencies for collection?

A. Yes.

Q. And in your experience as collector of accounts, is it your opinion that a diligent effort was made to collect these accounts prior to this sale on October 2, 1936?

Mr. Hiken: I object.

A. Yes.

Mr. Hiken: It if please Your Honor, ask it be stricken, what the opinion of this witness is as to what efforts were made to collect the money.

By Mr. Sovik:

Q. Tell us what was done, Miss Pellenz?

The Member: Objection is sustained.
Mr. Sovik: I will withdraw that question.

By Mr. Sovik:

Q. Tell us what was done in connection with that?
A. In connection with the collecting the accounts?
Q. What effort was made by you and others within your knowledge?

The Member: Anything that you know about yourself.

A. Well, we made a very exhaustive survey of the accounts and brought our charges up to date and got bills out and tried our very best to clean up just as many of them as we possibly could.

By Mr. Sovik:

Q. To refresh your recollection, were some of those turned over to various collection agencies?
A. Yes. In the process of trying to collect them we turned over an account.
[fol. 42] Q. To the Syracuse Collection Agency, Boyd Service Collection Agency——
A. Yes.
Q. —and the Empire Collection Service?
A. Yes.
Q. What is known as the Physicians' Discount Service?
A. That is right.
Q. I show you Exhibit 3 marked for identification and ask you to state whether or not that is the paper writing purporting to be the assignment or the bill of sale of these accounts receivable which you have testified were sold on October 2, 1936?
A. Yes, this is.

Mr. Sovik: I offer it in evidence.
The Member: Received in evidence. Is there any objection?
Mr. Hiken: I don't know, Your Honor, I haven't seen it. May I have a moment to look at it?
The Member: The witness identified it.

Mr. Hiken: Well, I don't know if her identification of this is at all proper. I don't know by whom it was drawn or signed.

Counsel examines document.

Mr. Hiken: No objection, Your Honor.

The Member: Received as petitioner Exhibit 3.

The said document (assignment) so offered and received in evidence, was marked petitioner's Exhibit 3, and made a part of this record.

Mr. Sovik: That is all, Your Honor.

Recross-examination.

By Mr. Hiken:

Q. Miss Pellenz, on the basis of the cash distributions made to the estate of Dr. Wallace in 1935 and in 1936, disregarding the distribution made on account of this sale, what is the portion of the accounts receivable owing to these firms in the amount of $69,601.13, as of the date of Dr. Wallace's death, which was actually collected?

[fol. 43] Mr. Sovik: Your Honor, I want to object to that as being improper in form and not the best evidence. The partnership agreements are in evidence and they tell what the distributive share should be.

The Member: Objection overruled. Exception is noted for the petitioner.

A. If I understand your question, you want to know the percentage. Will you repeat that again?

The Member: Let the reporter read the question.

(Whereupon the reporter read the question as recorded.)

A. And do you mean what proportion is that amount which was paid to Dr. Wallace without that five hundred dollars of $61,000, what proportion of that amount was paid?

By Mr. Hiken:

Q. How much of that amount owing to these firms of these accounts receivable?

A. By these "firms" you mean the two partnerships?

Q. The two partnerships.

A. Oh, the two partnerships.

Q. The accounts receivable owing to the two partnerships as of the date of Dr. Wallace's death, how much was actually collected before——

A. Before the sale?

Q. —before the sale of certain uncollected accounts?

A. Yes. Well, I read off that figure, that was the figure of $16,251.21 was collected in cash.

Q. That was the amount actually collected in cash?

A. Yes.

The Member: That $16,000 odd was collected, and that was collected on account of the accounts receivable in the sum of $69,000 odd that existed as of Dr. Wallace's death, is that what you mean?

The Witness: That is correct, that is what I am trying to say.

[fol. 44] Mr. Hiken: Will Your Honor excuse me while I make a little computation here. May I see petitioner's Exhibit 3, please?

The Member: The Board will recess for a few minutes.

(Thereupon a recess was taken for a few minutes, at the end of which the following occurred:)

Mr. Hiken: I have no further questions.

Mr. Sovik: I have nothing further.

The Member: Anything on the part of the respondent? Is that your entire case?

Mr. Sovik: Yes.

Mr. Hiken: We want to stipulate something from the estate tax return filed by the estate into the record.

STIPULATION

Mr. Sovik: We will stipulate, Your Honor, that the executors, petitioners in this proceeding, filed an estate tax and returned their interest in the partnerships which are set forth in Exhibits 1 and 2 in this case, of $6,693.14 as part of the gross estate of the decedent at the time of his death, and that that return was verified December 8, 1936, and filed with the department on December 21, 1936. I probably should have covered that in my opening statement, Your Honor. Further, that in this return the foregoing item of $6,693.14 is explained as follows: I will stipulate that

item number 1 in schedule F, which is made a part of that return, be made a part of the record in this proceeding.

Mr. Hiken: That may be marked as a joint exhibit.

The Member: A4.

The said document so offered and received in evidence was marked petitioner's and respondent's Exhibit A4, and made a part of this record.

[fol. 45] Mr. Hiken: And may I have leave to withdraw it and substitute a photostatic copy thereof?

The Member: That order has already been made.

Mr. Hiken: It is understood, as part of the record, that joint Exhibit A4 is an explanation of an item which, it has already been stipulated, was included as an asset in the gross estate of the decedent, Dr. Wallace, in the estate tax return filed by his estate.

The Member: Anything further on the part of respondent?

Mr. Hiken: I would like to point out for the purpose of the record, with Your Honor's permission, that the amount of the decedent's distributable share in the accounts receivable, at the time of his death, is stated in the deficiency notice to be $5,689.19.

The Member: We follow that. We were going to ask you how you reached that figure?

Mr. Hiken: I don't know exactly how that figure was reached, Your Honor. However, it is considerably less than the amount set forth in the estate tax return as representing the decedent's interest in these accounts receivable at the date of his death and is also less than the amount that Miss Pellenz testified to as having actually been paid in cash out of the accounts receivable which were collected. Those amounts, exclusive of the five hundred dollars from the sale of certain accounts, total $6,125.76. Because the lesser amount is stated in the deficiency notice, however, the respondent does not request any increase in that amount, and if Your Honor finds that the situation is within section 42 and that those amounts are properly accrueable to petitioner and should have been included in his income on the income tax return filed for the decedent for the year of [fol. 46] his death, the partnership income to be included is limited to the small amount set forth in the deficiency notice.

I would like also to point out to Your Honor, which is just an explanation of an amount which is stated, that in

the deficiency notice, items of interest and taxes accrued at the date of the decedent's death were allowed as deductions. Those deductions have not been claimed in the return. Those deductions are set forth as items 4 and 5 at the bottom of page 1 of the statement attached to the deficiency notice and explain the discrepancy in the amounts testified to here today and the amounts set forth in the deficiency notice.

EXHIBIT "1"

Articles of Agreement made and entered into this 1st day of July, 1933, by and between William L. Wallace, Herbert O. Brust, Carl E. Muench and Carlton F. Potter, severally of the City of Syracuse, Onondaga County, New York, Witnesseth:

First: In consideration of the mutual promises and agreements herein contained the said parties above named have agreed to become co-partners in the practice of medicine under the firm name and style of "Wallace, Brust, Muench & Potter," and by these presents do become co-partners in the practice of medicine in the City of Syracuse and elsewhere, under the firm name and style of "Wallace, Brust, Muench & Potter."

Second: That said co-partnership shall commence on July 1st, 1933, and end on June 30, 1935.

Third: To the end and purpose of this agreement each party agrees to give his whole time and attention to the affairs of said co-partnership, and to perform in the discharge of his duties such work as may be properly assigned to him.

[fol. 47] Fourth: At all times during the continuance of this co-partnership each of the parties hereto agree to give their attention and to their and each of their best endeavors to put the utmost of their skill and power exerting themselves for their joint interest, profit, benefit and advantage. Each party hereto agrees that he shall and will at all times during said co-partnership bear, pay and discharge between them all costs and expenses that may be required for the support and management of said co-partnership business and that all gains, profits and increases that shall come,

grow and arise by means of their said business and profession shall be divided between them, and all losses that shall in any manner happen to said business shall be borne and paid by them in the following proportion, i. e., the shares of each of said partners shall be in the following proportion during each of the two years of said agreement:

William L. Wallace, twenty-six seventy-seconds (26/72) part of all profits and losses incident to said co-partnership; Herbert O. Brust, fifteen seventy-seconds (15/72) part of all profits and losses incident to said co-partnership; Carl E. Muench, eleven seventy-seconds (11/72) part of all profits and losses incident to said co-partnership; and Carl F. Potter, twenty seventy-second (20/72) part of all profits and losses incident to said co-partnership.

Fifth: It is understood and agreed that any and all moneys hereafter received on account of the previous agreements of co-partnership between the parties hereto shall be divided on the ratio stated herein, and all debts, liabilities and charges of every kind accruing previous to July, 1933, on account of the aforesaid co-partnership agreements shall be paid by the parties hereto in the same ratio.

Sixth: It is agreed that there shall be had and kept at all times during the continuance of this co-partnership, perfect, [fol. 48] just and true books of account wherein each of said co-partners shall enter and set down all money by them or either of them, received, paid out and expended in and about said business, and also all goods, wares and commodities and merchandise by them or either of them bought or sold on account of said co-partnership business whatsoever. Said books shall be used in common between the said co-partners and each may have access thereto without interruption or hindrance of the other.

Seventh: All moneys received during the term of this co-partnership agreement shall be deposited in the Merchants National Bank and Trust Company under the firm name of "Wallace, Brust, Muench & Potter", and each party of said firm shall be allowed to draw checks upon said funds.

Eighth: That on the first day of each month hereafter until and including July 1, 1935, there shall be an accounting at the end of each month of all of the partnership gains and losses, and there shall be paid to each of said partners,

after the deduction of the expenses of said co-partnership, the proportionate share of the profits of said co-partnership as hereinbefore specified. The losses sustained by said co-partnership during said term shall be borne by each of said co-partners in the same proportion as hereinbefore provided.

Ninth: It is understood and agreed that nothing herein contained shall in any way prevent any or either of the parties hereto from carrying health and accident insurance for their own individual benefit but at their own cost and expense.

Tenth: It is also agreed that each man at his own cost will maintain his own separate automobile or automobiles as he may see fit or his work requires, and pay the expenses incident to the maintenance of the same, except such partner hereto may charge said co-partnership with the expense for all necessary out of town business trips taken in the in- [fol. 49] terest of said co-partnership, at the rate of six cents per mile for all business trips taken by automobile. Each man shall maintain in his own home or residence at his own expense, a telephone.

Eleventh: It is agreed that the members of said co-partnership shall not make or endorse any note, or procure money upon the written promise of said co-partnership, or discount any notes or other obligations of said co-partnership, but nothing herein is intended to limit or abridge the right of each member of said co-partnership to sign checks for the withdrawal of money and to endorse for deposit checks, notes or other evidences of debt in the conduct of said partnership.

Twelfth: Any one of the parties to this contract may terminate this co-partnership agreement upon sixty (60) days' written notice of his intention so to do, delivered personally to the other parties to this agreement on the first day of the month. Each monthly settlement of the partnership gains and losses between the parties hereto, their heirs, executors, administrators and assigns, shall constitute an accord and satisfaction of all claims against said co-partnership which each party hereto has against the other on account of said co-partnership, and a full accounting to such date. The last monthly settlement shall constitute an accord and satisfaction, a release and discharge to

that date of all claims which each member of this co-partnership has against the other.

Thirteenth: It is also agreed that at the end or sooner termination of this co-partnership each co-partner shall and will make a just, true and final account of all things relating to said business and that all things will be adjusted and all gains and increases thereof shall appear to be remaining either in money, goods, wares or merchandise, debts or otherwise shall be divided between them, and all outstanding book accounts shall be collected at the end of the said co-partnership by them, and that all proceeds realized [fol. 50] from the collection thereof, less the actual expenses incident to the collection thereof, shall be divided between them, and all outstanding book accounts shall be collected at the end of the said co-partnership by them, and that all proceeds realized from the collection thereof, less the actual expense incident to the collection thereof, shall be divided between the members of the co-partnership as follows:

William L. Wallace, twenty-six seventy-seconds (26/72) part of all profits and losses incident to said co-partnership; Herbert O. Brust, fifteen seventy-seconds (15/72) part of all profits and losses incident to said co-partnership; Carl E. Muench, eleven seventy-seconds (11/72) part of all profits and losses incident to said co-partnership; and Carlton F. Potter, twenty seventy-seconds (20/72) part of all profits and losses incident to said co-partnership.

Fourteenth: This agreement is binding upon the heirs, executors, administrators and assigns of the parties hereto.

In Witness Whereof the said parties have hereunto set their hands and seals this 1st day of July, 1933.

William L. Wallace, L. S. Herbert O. Brust, L. S.
Carl E. Muench, L. S. Carlton F. Potter, L. S.

EXHIBIT "2"

Articles of Agreement made and entered into this 1st day of July, 1935, by and between William L. Wallace, Herbert O. Brust, Carl E. Muench, Carlton F. Potter and Alvin J. [fol. 51] Spire, severally of the City of Syracuse, Onondaga County, New York, Witnesseth:

First: In consideration of the mutual promises and agreements herein contained the said parties above named have agreed to become co-partners in the practice of medicine under the firm name and style of "Wallace, Brust, Muench, Potter & Spire", and by these presents do become co-partners in the practice of medicine in the City of Syracuse and elsewhere, under the firm name and style of "Wallace, Brust, Muench, Potter & Spire."

Second: That said co-partnership shall commence on July 1st, 1935, and end on June 30, 1936.

Third: To the end and purpose of this agreement each party agrees to give his whole time and attention to the affairs of said co-partnership, and to perform in the discharge of his duties such work as may be properly assigned to him.

Fourth: It is understood and agreed that any and all moneys hereafter received on account of the previous agreement dated July 1, 1933 on account of a co-partnership between William L. Wallace, Herbert O. Brust, Carl E. Muench and Carlton F. Potter, after the payment of all debts, liabilities and charges to July 1, 1935, on account of the aforesaid partnership agreement shall belong exclusively to William L. Wallace, Herbert O. Brust, Carl E. Muench and Carlton F. Potter and shall be devided on the following ratio:

William L. Wallace	26/72nds
Herbert O. Brust	15/72nds
Carl E. Muench	11/72nds
Carlton F. Potter	20/72nds

[fol. 52] Fifth: That during the continuance of this agreement William L. Wallace, Herbert O. Brust, Carl E. Muench, Carlton F. Potter and Alvin J. Spire agree to devote their time and attention and best endeavors to the utmost of their skill and power for the interest, benefit and profit as herein provided. That the entire professional receipts during said term paid to and received by William L. Wallace, Herbert O. Brust, Carl E. Muench, Carlton F. Potter and Alvin J. Spire shall be paid into a common fund and from said fund there shall be paid the following:

(1) All professional business expenses of each of said parties as herein defined.

(2) Joint expenses of said Wallace, Brust, Muench, Potter & Spire, if any.

(3) To Herbert O. Brust a sum sufficient which when added to the amount received from Wallace, Brust, Muench & Potter under the Fourth paragraph above will equal a total amount of $100.00 a week.

(4) After making the payments and deductions aforesaid the balance remaining from said gross income shall be divided into one hundred equal parts and shall be monthly set aside and paid over to the following named persons and in the following proportions:

William L. Wallace, forty one-hundredths (40/100) part of all profits and losses incident to said co-partnership;

Carl E. Muench, fifteen one-hundredths (15/100) part of all profits and losses incident to said co-partnership;

Carlton F. Potter, thirty one-hundredths (30/100) part of all profits and losses incident to said co-partnership;

Alvin J. Spire, fifteen one-hundredths (15/100) part of all profits and losses incident to said co-partnership.

[fol. 53] Sixth: It is understood and agreed that there shall be had and kept at all times during the continuance of this co-partnership, perfect, just and true books of account wherein each of said co-partners shall enter and set down all moneys by them or either of them received, paid out and expended in and about said business, and also all goods, wares and commodities and merchandise by them or either of them bought or sold on account of said co-partnership business whatsoever. Said books shall be used in common between the said co-partners and each may have access thereto without interruption or hindrance of the other.

Seventh: All moneys received during the term of this co-partnership agreement shall be deposited in the Merchants National Bank and Trust Company under the firm name of "Wallace, Brust, Muench, Potter & Spire", and each party of said firm shall be allowed to draw checks upon said funds.

Eighth: That on the first day of each month hereafter, until and including July 1, 1936, there shall be an accounting for the preceding month of all of the partnership gains and losses, and there shall be paid to each of said partners, after

the deduction of the expenses of said co-partnership, the proportionate share of the profits of said co-partnership as hereinbefore specified.

Ninth: It is understood and agreed that nothing herein contained shall in any way prevent any or either of the parties hereto from carrying health and accident insurance, for their own individual benefit, but at their own cost and expense.

Tenth: It is also agreed that each man at his own cost will maintain his own separate automobile or automobiles as he may see fit or his work requires, and pay the expenses incident to the maintenance of the same, except such partner hereto may charge said co-partnership with the expense [fol. 54] for all necessary out-of-town business trips taken in the interest of said co-partnership, at the rate of six cents per mile for all business trips taken by automobile. Each man shall maintain in his own home or residence, at his own expense, a telephone.

Eleventh: It is agreed that the members of said co-partnership shall not make or endorse any note, or procure money upon the written promise of said co-partnership, or discount any notes or other obligations of said co-partnership, but nothing herein is intended to limit or abridge the right of each member of said co-partnership to sign checks for the withdrawal of money and to endorse for deposit checks, notes or other evidences of debt in the conduct of said partnership.

Twelfth: Any one of the parties to this contract may terminate this co-partnership agreement upon thirty (30) days' written notice of his intention so to do, delivered personally to the other parties to this agreement on the first day of the month. Each monthly settlement of the partnership gains and losses between the parties hereto, their heirs, executors, administrators and assigns, shall constitute an accord and satisfaction of all claims against said co-partnership which each party hereto has against the other on account of said co-partnership, and a full accounting to such date. The last monthly settlement shall constitute an accord and satisfaction, a release and discharge to that date of all claims which each member of this co-partnership has against the other.

Thirteenth: It is also agreed that at the end or sooner termination of this co-partnership each co-partner shall and will make a just, true and final account of all things relating to said business and that all things will be adjusted and all gains and increases thereof shall appear to be remaining either in money, goods, wares or merchandise, [fol. 55] debts or otherwise shall be divided between them, and all outstanding book accounts shall be collected at the end of the said co-partnership by them, and that all proceeds realized from the collection thereof, less the actual expenses incident to the collection thereof, shall be divided between them, and all outstanding book accounts shall be collected at the end of the said co-partnership by them, and that all proceeds realized from the collection thereof, less the actual expense incident to the collection thereof, shall be divided between the members of the co-partnership as follows:

William L. Wallace, forty one-hundredths (40/100) part of all profits and losses incident to said co-partnership;

Carl E. Muench, fifteen one-hundredths (15/100) part of all profits and losses incident to said co-partnership;

Carlton F. Potter, thirty one-hundredths (30/100) part of all profits and losses incident to said co-partnership;

Alvin J. Spire, fifteen one-hundredths (15/100) part of all profits and losses incident to said co-partnership.

Fourteenth: This agreement is binding upon the heirs, executors, administrators and assigns of the parties hereto.

In Witness Whereof, the said parties have hereunto set their hands and seals this — day of July, 1935.

William L. Wallace, L.S.; Herbert O. Brust, L.S.; Carl E. Muench, L.S.; Carlton F. Potter, L.S.; A. J. Spire, L.S.

(Acknowledged July 24, 1935)

[fol. 56] EXHIBIT "3"

Know All Men by These Presents, That Frank C. Wallace and Norman J. Pfaff, as executors of the estate of William L. Wallace, deceased, parties of the first part, in consideration of the payment to them as such executors of the sum of five hundred dollars ($500.00) by Frederic A. Lyman,

of Syracuse, New York, party of the second part, the receipt whereof is hereby acknowledged, have sold and by these presents do grant, assign and convey unto the said Frederic A. Lyman, a one-fifth interest of William L. Wallace, deceased, in the accounts receivable of a certain partnership known as Wallace, Brust, Muench, Potter & Spires remaining due and unpaid, as set forth in Exhibit "A" hereto annexed and made a part hereof.

To Have and to Hold the same unto the said Frederic A. Lyman, his heirs, executors, administrators and assigns forever, to and for the use of the said Frederic A. Lyman, hereby constituting and appointing the said Frederic A. Lyman their true and lawful attorney, irrevocably in their name, place and stead for the purpose aforesaid, to ask, demand, sue for, attach, levy, recover and receive all such sum and sums of money which now are or may hereafter become due, owing and payable for or on account of all and any of the accounts, dues, debts and demands above assigned, giving and granting unto the said attorney full power and authority to do and perform all and every act and thing whatsoever requisite and necessary as fully to all intents and purposes as they might or could do if personally present, with full power of substitution and revocation, hereby ratifying and confirming all that the said attorney or his substitute shall lawfully do or cause to be done by virtue hereof.

[fol. 57] The aforesaid assignment and transfer being made in furtherance of a public sale of the subject of this assignment held pursuant to a decree of the Surrogate's Court of the County of Onondaga dated September 16, 1936, which sale was held on October 2, 1936, at eleven o'clock in the forenoon of that day, at 930 University Building, Syracuse, New York, and the aforesaid assignee having been the highest bidder at said sale.

In Witness Whereof the parties of the first part have hereunto set their hands and seals this 16th day of October, 1936.

Frank B. Wallace, Norman J. Pfaff, Executors of the Estate of William L. Wallace, Deceased.

(Acknowledged Oct. 16, 1936.)

EXHIBIT "A4"

Schedule F

1. Interest in partnerships, con'td.:

Deceased had an interest in the partnership of Wallace, Brust, Muench & Potter, which partnership existed until July 1, 1935, in which deceased's share in the partnership accounts was 26/72.

Deceased also had an interest in the partnership of Wallace, Brust, Muench, Potter & Spires, which partnership existed from July 1, 1935, to Dec. 25, 1935, in which deceased's share in the partnership accounts was 40/100.

[fol. 58] The net earnings of said partnerships for the five years preceding date of death are as follows:

1931	1932	1933	1934	1935
$69,455.10	$49,881.13	$49,317.94	$51,100.00	$53,524.40

These partnerships were formed by physicians associated with Crouse-Irving Hospital, Syracuse, N. Y., and the only asset of any value in said partnerships were the accounts receivable in which deceased's share was as explained above.

The value of deceased's share as of the date of his death in these accounts is accurately determined by the amount of payments which have been made to the Executors on the same from the date of death to Oct. 1, 1936, namely—$6,193.14, at which time the remaining accounts were sold by the Executors under an order of the Surrogate's Court of Onondaga County to Frederic A. Lyman for the sum of $500.00, making the total value of these assets $6,693.14.

BEFORE UNITED STATES BOARD OF TAX APPEALS

STIPULATION AS TO PRINTED RECORD

It is hereby stipulated that the Clerk may omit from the printed record the Table of Contents and the colloquy of counsel contained in pages 1 through 9, and the last 13 lines on page 46, and page 47 of the Transcript of Minutes, and also the Schedule of Accounts annexed to Exhibit 3.

Laurence Sovik, Attorney for Petitioner. Samuel O. Clark, Jr., Attorney for Respondent.

April 16th, 1940.

[fol. 59] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 60] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, OCTOBER TERM, 1939

No. 337

(Argued June 12, 1940. Decided July 8, 1940)

NORMAN J. PFAFF and FRANK B. WALLACE, Executors of Estate of William L. Wallace, Deceased, Appellants,

vs.

COMMISSIONER OF INTERNAL REVENUE, Appellee

On Petition for Review from the United States Board of Tax Appeals

Before Swan, Augustus N. Hand and Patterson, Circuit Judges

Laurence Sovik, Attorney for Appellants; Costello, Cooney & Fearon, of Counsel.

Samuel O. Clark, Jr., Assistant Attorney General; Sewall Key and Morton K. Rothschild, Special Assistants to the Attorney General, for Appellee.

OPINION

Per CURIAM:

Decision affirmed.

[fol. 61] IN UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT

NORMAN J. PFAFF and FRANK B. WALLACE, as Executors, etc., Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Appeal from the United States Board of Tax Appeals

JUDGMENT—Filed July 24, 1940

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals, and was argued by counsel.

On Consideration Whereof, it is now hereby ordered, adjudged, and decreed that the order of said United States Board of Tax Appeals be and it hereby is affirmed.

It is further ordered that a Mandate issue to the said Board in accordance with this decree.

D. E. Roberts, Clerk.

[fol. 62] [File endorsement omitted.]

[fol. 63] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 64] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed November 12, 1940

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted, and the case is assigned for argument immediately following No. 436.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on Cover: File No. 44,828. U. S. Circuit Court of Appeals, Second Circuit. Term No. 479. Norman J. Pfaff and Frank B. Wallace, Executors of the Estate of William L. Wallace, Deceased, Petitioners, vs. Commissioner of Internal Revenue. Petition for a writ of certiorari and exhibit thereto. Filed October 1, 1940. Term No. 479, O. T., 1940.

No. 479

In the Supreme Court of the United States

OCTOBER TERM, 1940

NORMAN J. PFAFF and FRANK B. WALLACE, Executors of Estate of William L. Wallace, Dec'd,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

LAURENCE SOVIK,
Attorney for Petitioners,
Office and P. O. Address,
930 University Block,
Syracuse, New York.

COSTELLO, COONEY & FEARON,
Of Counsel,
930 University Block,
Syracuse, New York.

SYRACUSE TYPESETTING CO., INC., 321 W. FAYETTE STREET, SYRACUSE, N. Y.

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FOR THE SECOND CIRCUIT

NORMAN J. PFAFF and FRANK B. WALLACE, Executors of Estate of WILLIAM L. WALLACE, Dec'd,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

Laurence Sovik, Esq., on behalf of Norman J. Pfaff and Frank B. Wallace, Executors of the Estate of William L. Wallace, deceased, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Second Circuit, entered in the above entitled action on July 8th, 1940.

OPINIONS BELOW

The opinion of the Board of Tax Appeals was a memorandum opinion (Fols. 31-41) and was not officially reported. The decision of the Circuit Court of Appeals was reported at 113 Fed. (2d.) 114. It likewise was a memorandum decision.

JURISDICTION

The jurisdiction of this Court to review this decision is derived from Section 240 of the Judicial Code as amended (28 U. S. C. A., §347), wherein this Court is authorized upon the petition of any party to require by certiorari either before or after a judgment or decree by such lower court, that the cause be certified to the Supreme Court for determination by it, with the same power and authority and with like effect as if the cause had been brought there by unrestricted writ of error or appeal.

This case involves the interpretation of Section 42 of the Revenue Act of 1934.

The decision which petitioners seek to have reviewed was handed down by the Circuit Court of Appeals for the Second Circuit on July 8, 1940.

STATEMENT

On August 30, 1937, the Commissioner notified petitioners that he had determined a deficiency in the tax return filed by petitioners for decedent for the year 1935 (Fols. 15-27). Petitioners duly filed a petition to the United States Board of Tax Appeals for a redetermination of the deficiency (Fols. 8-14) and a hearing thereon was had before Board Member J. Russell Leech, Esq., at Buffalo, N. Y., on June 20, 1939. On Sept. 30, 1939, a decision was rendered by Hon J. Russell Leech, affirming the Commissioner's determination (Fol. 42). Petitioners thereupon duly filed a petition for review by the United States Circuit Court of Appeals for the Second Circuit (Fols. 43-54). The appeal was argued before the Circuit Court, and on July 8, 1940, a decision was handed down, affirming without opinion the decision of the Board of Tax Appeals (Fol. 178).

Decedent, William L. Wallace, was a member of a partnership of practicing physicians. On July 1, 1933, decedent and several other physicians and surgeons entered into a partnership agreement (Ex. 1, Fols. 137-149) under which they operated until June 30, 1935. At that time the old partnership was dissolved and a new partner taken in and a new partnership agreement made, under which decedent and his associates operated until Dec. 25, 1935, when decedent died (Ex. 2, Fols. 150-165). Both of said partnerships were maintained on a cash basis, as were also the books of decedent (Fol. 95).

Petitioners filed an income tax return for the year 1935, the year in which decedent died, including therein all sums which decedent had received or was entitled to from the partnerships, according to the partnership agreements. In assessing the deficiency against petitioners, the Commissioner claimed that in decedent's return for 1935 they should have included his share of the estimated receipts from all cases which the partners were then treating, in spite of the fact that the monies had not been received by the partnership and that many of the cases were not completed or fees thereon fixed at the time of the decedent's death.

Some of these cases were completed during 1936 and the fees due were collected by the surviving partners. Decedent's share of the sums so collected, amounting to $5,189.19, was paid over to decedent's estate by the surviving partners during 1936 (Fols. 134, 135). On Oct. 1, 1936, decedent's interest in the uncollected accounts was sold at public auction, pursuant to order of the Surrogate of Onondaga County, for $500 (Ex. 3, Fol. 166).

The partnership agreement specifically provided that the partnership accounts should be maintained on a cash basis and that a partner was not entitled to share in the proceeds of cases

being treated until the fees had been collected and partnership expenses paid therefrom. Thus paragraph Eighth (Fols. 143, 158) of the agreements (Exs. 1 and 2) provide that on the first day of each month there shall be an accounting for the preceding month of—

> "all partnership gains and losses and there shall be paid to each of said partners, after the deduction of the expenses of said partnership, the proportionate share of the profits of said co-partnership, as hereinbefore specified."

And paragraph Sixth (Fols. 142, 157) of the agreements (Exs. 1 and 2) provide that the books of account of the partnership shall contain a record of—

> "all money by them or either of them received, paid out or expended in and about said business."

No entries were made on the partnership books until the money for the particular service had been received by the partnerships (Fols. 94, 96). A record of services to patients was maintained on a card system (Fol. 98). As services were rendered an entry was made on one of these cards to show the time and amount of service performed (Fols. 98, 100). No bills were sent out until the case was completed (Fol. 98), and in many cases no charge was ever made and no bill ever sent (Fol. 99). Upon the completion of the case, the physician partner in charge thereof, made a flat charge for the entire case and a bill was then sent out to the patient (Fols. 96, 100).

The books of the partnership showed only expenditures actually made and cash actually received (Fol. 95). The monthly accounts had, pursuant to paragraph Eighth of each of the partnership agreements, referred only to the cash transactions appearing on the books.

It is petitioners' contention that the Commissioner erred in holding that the value of the cases under treatment by the various partners constituted income to decedent which might be accrued under Section 42 of the Revenue Act.

THE QUESTION PRESENTED

Whether the unallocated share of a partner in the prospective receipts from services performed by the partnership prior to his death constitutes income to decedent which may be accrued under Section 42 of the Revenue Act of 1934, when both the deceased partner and the partnership maintain their books on a cash basis.

STATUTES AND REGULATIONS INVOLVED

Revenue Act of 1934, C. 277, 48 Stat. 680:

> "Sec. 4. The application of the General Provisions and of Supplements A to D, inclusive, to each of the following special classes of taxpayers, shall be subject to the exceptions and additional provisions found in the Supplement applicable to such class, as follows:
>
> (a) Estates and trusts and the benficiaries thereof, Supplement E.
>
> (b) Members of partnerships,—Supplement F.
>
> (c) Insurance companies,—Supplement G.
>
> (d) Nonresident alien individuals,—Supplement H.
>
> (e) Foreign corporations,—Supplement I.
>
> (f) Individual citizens of any possession of the United States who are not otherwise citizens of the United States and who are not residents of the United States,—Supplement J.
>
> (g) Individual citizens of the United States or domestic corporations, satisfying the conditions of Section 251 by reason of deriving a large portion of their

gross income from sources within a possession of the United States,—Supplement J.

(h) China Trade Act corporations,—Supplement K."

(U. S. C., Title 26, §4.)

"Sec. 42. Period in which items of gross income included.

The amount of all items of gross income shall be included in the gross income for the taxable year in which received by the taxpayers, unless, under the methods of accounting permitted under Section 41, any such amounts are to be properly accounted for as a different period. In the case of the death of a taxpayer there shall be included in computing net income for the taxable period in which falls the date of his death, amounts accrued up to the date of his death if not otherwise properly includible in respect of such period or a prior period (U. S. C., Title 26, Sec. 42)."

"Sec. 181. Partnership not taxable.

Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity (U. S. C., Title 26, Sec. 181)."

"Sec. 182. Tax of partners.

There shall be included in computing the net income of each partner his distributive share, whether distributed or not, of the net income of the partnership for the taxable year (U. S. C., Title 26, Sec. 182)."

Treasury Regulations, 86, relating to the Revenue Act of 1934, Art. 42-2, provides:

"Income not reduced to possession—Income which is credited to the account of or set apart for a taxpayer and which may be drawn upon by him at any time is

subject to tax for the year during which so credited or set apart, although not then actually reduced to possession. To constitute receipt in such a case the income must be credited or set apart to the taxpayer without any substantial limitation or restriction as to the time or manner of payment or condition upon which payment is to be made, and must be made available to him so that it may be drawn at any time, and its receipt brought within his own control and disposition * * *." .

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that decedent's share in the prospective receipts for services rendered by the partnership of which he was a member prior to the date of his death but not then received either by the partnership nor by the partner, should be considered income to decedent in year 1935 accruable within the meaning of Section 42 of the Revenue Act of 1934.

2. In failing to hold that decedent's share in the prospective receipts for services rendered by the partnership of which he was a member prior to the date of his death but not then received either by the partnership nor by the partner, did not constitute income to decedent in year 1935.

3. In affirming the decision of the Board of Tax Appeals.

REASONS RELIED UPON FOR WRIT

1. The decision of the Circuit Court of Appeals for the Second Circuit, affirming the commissioner's action in assessing the deficiency against petitioners, conflicts with the decisions of other Circuit Courts of Appeal.

By its memorandum opinion in the instant case, reported at 113 Fed. (2d) 114, the Second Circuit Court of Appeals held that petitioners were required to report as decedent's income during 1935 his share of the accounts due the partnership of which he was a member, even though the partnership had not collected these accounts, nor allocated to any partner his particular share, and in many instances the services had not been completed.

The Commissioner of Internal Revenue, in making this assessment, relied upon §42 of the Revenue Act of 1934, which provides in part:

> "In the case of the death of a taxpayer there shall be included in computing net income for the taxable period in which falls the date of his death amounts accrued up to the date of his death if not otherwise properly includable in respect of such period or a prior period."

The Commissioner contends that this section authorized him to include in decedent's income for the year 1935 the value of the cases then being treated by the partnership of physicians of which decedent was a member. Some of these accounts were collected during 1936; decedent's interest in the balance was sold at auction during that year. The partnership kept its accounts on a cash basis, as did decedent. The partnership agreements expressly provided that the individual partners should receive from the partnership only their respective shares of the cash received.

In making the assessment the Commissioner interpreted §42, which provides for the accrual of the income of a deceased taxpayer up to the date of his death, to require the accrual

of the income of a partnership of which decedent was a member, even though the partnership had maintained its accounts on a cash basis.

The Commissioner's interpretation was sustained by the Board of Tax Appeals in a memorandum decision which was affirmed by the Circuit Court of Appeals for the Second Circuit at 113 Fed. (2d) 114. This decision by the Circuit Court is in direct conflict with the decision reached by the Circuit Court of Appeals for the Third Circuit in an almost identical case, *Enright's Estate vs. Commissioner of Internal Revenue*, 112 Fed. (2d) 919.

In that case decedent was a member of a partnership of lawyers which kept its accounts and made its tax returns on a cash receipts and disbursements basis. Their partnership agreement provided for the annual determination of the earnings to be distributed to the partners on the basis of cash receipts and disbursements. Decedent likewise made his returns on a cash basis. Decedent's distributable interest in the partnership cash was reported by his executors in the return filed subsequent to his death. The Commissioner added to decedent's taxable income his interest in the collectible accounts receivable of the firm and in fees earned in whole or in part not yet billed or received from clients, contending the same to be amounts accrued up to the date of his death and taxable in the year of his death. The Commissioner was sustained by the Board of Tax Appeals. The Circuit Court of Appeals for the Third Circuit, however, reversed, stating:

> "The Board said in its memorandum opinion that the effect of the provision of Section 42 of the Revenue Act which we have quoted above 'was to require that deceased be placed upon an accrual basis at the

date of his death. We agree that this was its effect. It follows that the decedent's taxable income should have been computed in the same way it would have been had he been alive and regularly making his returns on the accrual basis.

We think the Board fell into error in failing to treat the partnership as a tax computing unit separate from its member, Enright. That the Revenue Act requires that a partnership be so treated is clear from its provisions for the computing of partnership income and the filing of partnership returns and has been recognized by the courts. Thus a partnership may make its returns for a taxable year different from that of its members, and it may likewise make its returns upon an accounting basis different from that used by the individual partners."

The similarity between the above case and the case at bar is clear. The decision reached by the respective Circuit Courts are clearly at variance. Rule 38, subdivision 5(b) sets out as one of the bases for granting certiorari a decision of a Circuit Court of Appeals in conflict with the decision of another Circuit Court of Appeals on the same matter. This Court has likewise granted certiorari many times in cases where the decisions of Circuit Courts of Appeal conflict. (*Aschenbrenner v. U. S. F. & G. Co.*, 292 U. S. 80, 82; *Stroehmann v. Mutual Life Insurance Co.*, 300 U. S. 435, 440.) Mr. Chief Justice Taft stated in *Magnum Co. v. Coty*, 262 U. S. 159, 163:

"The jurisdiction to bring up cases by certiorari from the Circuit Courts of Appeal was given for two purposes, first to secure uniformity of decision between those courts and the nine Circuit Courts, and,

second, to bring up cases involving questions of importance which it is in the public interest to have decided by this Court of last resort."

Petitioners contend, therefore, that in order to secure uniformity of decision among the various Circuit Courts of Appeal this Court should grant a writ of certiorari in the present case.

2. The Circuit Court of Appeals for the Second Circuit has herein decided an important question of federal law which has not been but should be settled by this court.

The instant case is one of the first arising under the amendment which was added to Section 42 of the Revenue Act of 1934.

A decision by this Court upon this point is essential in view of the numerous cases in which this statute is and will be involved. Upon the decision in this case will rest the determination of the tax to be assessed against members of countless partnerships throughout the United States. Among professional men the partnership is the prevalent form of business association. To include as income to the deceased member of a partnership his respective share of the accounts of the partnership, whether collected or not, whether the work has been completed or not, would be to impose upon such taxpayer a burden certainly not intended by Congress in enacting the amendment in question.

Petitioners contend that the income intended to be reached by this statute is that which has accrued to decedent, not that which has accrued to the partnership of which he is a member.

That Section 42 of the Revenue Act was not intended to be interpreted as the Commissioner has done is clear from the very arrangement of the statute itself.

By the terms of Section 4, the general provisions of the Act are declared subject to special provisions in the Act for certain classes of taxpayers. Section 42, the interpretation of which is herein involved, is included in the title "General Provisions." Section 182 is the special provision for partnerships to which we are referred by Section 4.

By the terms of Section 182 the net income of a partner is to include his distributive share of the partnership income for the year. Reference to paragraphs "Sixth" and "Eighth" of the partnership agreements (Fols. 142, 143, 157, 158) shows that the individual partner had no distributive share in the partnership income until collection had been made, expenses paid and monthly accounts completed. Paragraph "Thirteenth" (Fols. 147, 162) provides that upon termination of the partnership, the proceeds should be distributed as they were collected. Decedent, therefore, had no distributive share in the proceeds upon the dissolution of the partnership until collection had been made, according to the terms of the agreements.

The distinction between partnership income and individual partner's income for tax purposes has been made many times by the courts. It has been held that the Government cannot levy upon partnership assets because of a tax claim against an individual partner (*U. S. v. Kaufman*, 267 U. S. 408); a partner cannot offset personal non-capital losses against his distributive share of partnership non-capital gains (*Johnston v. Commissioner*, 86 Fed. (2d) 732); the partners and their partnership can have different fiscal years (*Guaranty Trust Co. v. Commissioner*, 303 U. S. 493), and the partners and their partnership

can have different methods of accounting (*Truman v. U. S.*, 4 F. Supp. 447; *Percival H. Truman*, 3 B T A 386; *W. J. Burns*, 12 B T A 1209; *Fritz Hill*, 22 B T A 1079).

Petitioners further contend that there was no income accruable to decedent as claimed by the Commissioner. In this regard this Court stated in *Guaranty Trust Co. v. Commissioner*, 303 U. S. 493:

> "Receipt of income or accrual of the right to receive it within the tax year is the test of taxability, not the time it has taken the taxpayer to earn it, nor the duration of his investments which have finally resulted in profit. *Lucas v. Alexander*, 279 U. S. 573.
>
> The Revenue Acts have consistently adhered to that policy in taxing the income of a partner. Since the partner is entitled to profits only upon a partnership accounting at the end of the accounting period, his profits become subject to income tax when and as they are thus ascertained."

Unless the income was actually received by decedent before his death, or the right to receive it had accrued to him at that time, under the rule in *Guaranty Trust Co. v. Commissioner*, supra, it was not taxable during that tax year. The Commissioner makes no contention that decedent received the income during 1935, nor that he was entitled to receive it; he maintains that under the foregoing sections it became taxable accrued income to taxpayers as of the date of decedent's death.

Other cases reaching the same conclusion are: *Simms Oil Co. v. Commissioner*, 74 Fed. (2d) 561; *Helvering v. Russian Finance and Construction Corp.*, 77 Fed. (2d) 324; *H. Liebes v. Commissioner*, 90 Fed. (2d) 932.

In *Commissioner v. Edwards Drilling Co.*, 95 Fed. (2d) 719, the Circuit Court for the Fifth Circuit reviewed several decisions of this Court, stating:

> "It is, of course, true as the Board points out that under the accrual method of accounting employed by petitioner, items must be accrued as income when the events occurred to fix the amount due and determine liability to pay. *United States v. Anderson*, 269 U. S. 422, 46 S. Ct. 131, 70 L. Ed. 347. Generally speaking, however, the income tax law is concerned, and its administration should deal only, with, realized losses, and realized gains. *Lucas v. American Code Co.*, 280 U. S. 445, 50 S. Ct. 202; 74 L. Ed. 538, 67 A. L. R. 1010. The taxpayer therefore is under no obligation to pay a tax on income he might never receive. *North American Oil Consolidated v. Burnet*, 286 U. S. 417, 52 S. Ct. 613, 76 L. Ed. 1197. A strained construction in administrative efforts to accrue income should be avoided."

Article 42-2 of Treasury Regulation 86 and which provides for the computation of income not reduced to possession, declares that to constitute income to the taxpayer, it must be credited or set apart to him without substantial limitation or restrictions and made available to him to be drawn upon at any time.

An analogy in support of the holding sought by petitioners is found in decisions involving the return of income impounded pending disposal of litigation. In one such case, *North American Oil Consolidated v. Burnet*, 286 U. S. 417, the court held impounded income taxable in the year in which it was actually received. Brandeis, J., stated:

> "The net profits were not taxable to the company as income of 1936 * * *. There was no constructive receipt of the profits by the company in that year, because at no time during the year was there a right in the company to demand that the Receiver pay over the money. Throughout 1916, it was uncertain as to who would be declared entitled to the profits. It was not until 1917, when the District Court entered a final decree vacating the Receivership and dismissing the bill, that the Company became entitled to receive the money. Nor is it material for the purposes of this case, whether the company's return was filed on cash receipts and disbursements basis or on the accrued basis. In neither event was it taxable in 1916 on account of income which it had not yet received and which it might never receive."

Although the Commissioner claims that his interpretation of Section 42 does not constitute taxing as income to decedent his share of the partnership assets, that is exactly what it amounts to in the case of a partnership of professional men. In such cases the chief asset of a partnership, aside from the individual abilities of the various partners, are the accounts. These accounts cannot under the cases previously cited be considered income for the reason that they are neither definitely ascertainable nor capable of distribution to the members of the partnership.

In the light of the foregoing cases, this question of Federal Law is clearly of the greatest importance and has not yet been settled by this Court.

CONCLUSION

It is therefore respectfully submitted that for the reasons above stated this petition for writ of certiorari should be granted.

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1940 — NO. 479

NORMAN J. PFAFF and FRANK B. WALLACE,
Executors of Estate of William L. Wallace,
Deceased,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit

BRIEF FOR PETITIONERS

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Respondent.

BRIEF FOR PETITIONERS

OPINIONS BELOW

The Board of Tax Appeals rendered a memorandum opinion which was not officially reported. The said opinion is printed in the record herein on pages 9 to 11. The Circuit Court of Appeals for the Second Circuit, in a memorandum reported in 113 Fed. (2d) 114, affirmed without opinion.

JURISDICTION

Petitioners invoke the jurisdiction of this Court pursuant to Sec. 240 of the Judicial Code, as amended (28 U. S. C. A., §347) wherein this Court is authorized upon the petition of any party to require by certiorari, either before or after a judgment or decree by such lower Court, that the cause be certified to the Supreme Court for determination by it with the same power and authority and with like effect as if the cause had been brought there by unrestricted writ of error or appeal.

The petition for this writ was presented to this Court Oct. 1, 1940, and was granted on Nov. 12, 1940.

STATEMENT

On August 30, 1937, the Commissioner notified petitioners that he had determined a deficiency tax for the year 1935 (R. 4). Petitioners duly filed their petition to the Board of Tax Appeals for a redetermination (R. 2). A hearing was had before Board Member J. Russell Leech on June 20, 1939. On Sept. 30, 1939, his decision was rendered, affirming the Commissioner's determination (R. 11). Petitioners duly filed a petition for review by the United States Circuit Court of Appeals for the Second Circuit (R. 12-15). The appeal was argued before the Circuit Court. On July 8, 1940, a decision was handed down, affirming without opinion the Board's decision (R. 48).

FACTS

On July 1, 1933, decedent, William L. Wallace, a physician and surgeon, and several other physicians and surgeons, entered into a partnership agreement (Ex. 1 [Adm., R. 17; Pr., R. 38-41]) under which they operated until June 30, 1935. At that time the old partnership was dissolved, a new partner taken in, and a new partnership agreement made, under which decedent and his partners operated until Dec. 25, 1935, when decedent died (Ex. 2 [Adm., R. 17; Pr., R. 41-45]). Both of said partnerships maintained their accounts on a cash basis, as were also the books of decedent (R. 26).

Petitioners filed for the year 1935, the year in which decedent died, an income tax return reporting for all sums which decedent had received or was entitled to receive from the partnerships according to the partnership agreements. In assessing the deficiency against petitioners, the Commissioner claimed

that in this return petitioners should have also included decedent's share of the estimated receipts from all cases which any of the surviving partners were then treating, despite the fact that the proceeds therefrom had not been received by the partnership during 1935; nor had the fees thereon been fixed at the time of decedent's death.

Some of these cases were completed during 1936, the fees then fixed, and collected by the surviving partners. Decedent's share of the sums so collected amounted to $5,189.19 and was paid over to his estate by the surviving partners during the year 1936 (R. 37). On Oct. 1, 1936, decedent's interest in the remaining uncollected accounts was sold at public auction for $500 pursuant to the order of the Surrogate of Onondaga County, the court having jurisdiction of decedent's estate (Ex. 8 [Adm., R. 34; Pr., R. 45, 46]).

These partnership agreements expressly provided that the partnership accounts should be kept on a cash basis and that no partner was entitled to share in the proceeds of the cases under treatment until the fees had been collected and partnership expenses paid therefrom.

No entries were made on the partnership books until the money for the particular service had been received by the partnership (R. 25, 26). A record of services to patients was maintained on a card system (R. 26, 27). As services were rendered an entry was made on one of these cards to show the time and amount of service performed (R. 27). No bills were sent out until the case was completed, and in many cases no charge was ever made and no bill ever sent out (R. 27). Upon the completion of a case, the physician-partner in charge thereof made a flat charge for the entire case and a bill was then sent out to the patient (R. 27).

The books of the partnership showed only expenses actually paid and cash actually received (R. 26). The monthly accountings had, pursuant to paragraphs "Eighth" of each of the partnership agreements, referred only to the cash transactions appearing on the partnership books.

Petitioners contend that decedent's proportionate share of the value of cases under treatment at the date of decedent's death, by the surviving partners, and decedent's distributable share received by petitioners from the surviving partners in 1936 was not taxable income for 1935, but rather taxable as part of decedent's gross estate and that these items did not "accrue" within the meaning of Sec. 42 of the Revenue Act of 1934.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that decedent's share in the receipts for services rendered by these partnerships prior to his death but not received by the partnerships until 1936, after his death, should be considered taxable income to decedent in the year 1935 accruable within the meaning of Sec. 42 of the Revenue Act of 1934.

2. In failing to hold that decedent's share in the receipts for services rendered by these partnerships prior to his death but not received by the partnerships until 1936, after his death, did not constitute taxable income to decedent in the year 1935.

3. In affirming the decision of the Board of Tax Appeals.

POINT I

Upon the dissolution of a partnership by the death of a partner, his interest in the partnership accounts is not taxable income as of the date of such dissolution.

The Commissioner has taxed as income for 1935, the year of decedent's death, the monies received by decedent's estate from the liquidation and collection of partnership accounts in 1936. The partnership was dissolved because of decedent's death.

The Commissioner claims the monies so received to be taxable income under the provisions of the following sections of the Revenue Act of 1934:

> "Sec. 182. Tax of Partners: There shall be included in computing the net income of each partner his distributive share, whether distributed or not, of the net income of the partnership for the taxable year."

> "Sec. 41. General Rule. The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made in accordance with such method as in the opinion of the Commissioner does clearly reflect the income. If the taxpayer's annual accounting period is other than a fiscal year as defined in Section 48, or if the taxpayer has no annual accounting period or does not keep books, the net income shall be computed on the basis of the calendar year. (For use of inventories, see Section 22 (c).)"

> "Sec. 42. Period in which Items of Gross Income Included. The amount of all items of gross income shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods

> of accounting permitted under Section 41, any such amounts are to be properly accounted for as of a different period. In the case of the death of a taxpayer there shall be included in computing net income for the taxable period in which falls the date of his death, amounts accrued up to the date of his death if not otherwise properly includable in respect of such period or a prior period."

It must be remembered that Sections 41 and 42, supra, are found in Part IV of Subtitle B of the Revenue Act, "General Provisions." This part of the Act is entitled "Accounting Periods and Methods of Accounting." Sec. 182, on the other hand, is in the Supplement devoted to "Taxes on Partners." The only logical conclusion, therefore, is that Sections 41 and 42 are devoted to accounting problems and that Section 182 lays down the law as to when the distributive share of a partner is taxable.

Section 4 of the Act provides in part:

> "Special Classes of Taxpayers: The application of the general provisions and of Supplements A to D, inclusive, to each of the following special classes of taxpayers, shall be subject to the exceptions and additional provisions found in the Supplement applicable to such class, as follows:
>
> (a) Estates and trusts and the beneficiaries thereof, —Supplement E.
>
> (b) Members of partnerships,—Supplement F.
>
> (c) Insurance Companies,—Supplement G. * * *."

Supplement F, referred to above, is the specific provision in the Act for the computation of the tax on a partner's distributive

share in the partnership profits, and Section 182 falls within that provision. By the very terms of the 1934 Act, therefore, Section 42 is clearly subordinated to Supplement F in matters involving taxes on members of partnerships.

It is clear that Congress did not intend by amending Section 42, supra, to in any way alter the existing law with reference to the taxability of net income to partners from partnerships. The amendment to Section 42 was intended to reach the individual whose salary or income was accrued to him on the books of the corporation or other entity employing him. In the event of his death prior to his withdrawal of such accrued salary or income from the corporation accounts, prior to the change in Section 42, there was no provision by which this item could be taxed as income. It constituted a deduction from the corporation's tax, was not income to decedent's executor and, not having been received by decedent in his lifetime, could not be taxed as income to him. This amendment was passed solely for the purpose of reaching such income. Clearly it was not intended to in any way change the existing law with reference to taxable income to members of partnerships.

The question is, therefore, whether on the dissolution of a partnership by the death of a partner his share in the partnership accounts is taxable as income. From the first enactment of the income tax law in 1913 until the amendment to Section 42 the Commissioner had not taken that position. Petitioners contend that Section 42 has in no way extended to the Commissioner that additional right.

In order, therefore, to determine whether these receipts constituted taxable income, we must determine whether they were decedent's "distributive share * * * of the net income of the partnership for the taxable year" 1935 within the meaning of Section 182.

Paragraphs "Eighth" of the partnership agreements provide that

> "on the first day of each month there shall be an accounting for the preceding month of * * * all partnership gains and losses and there shall be paid to each of said partners, after the deduction of the expenses of said partnership, the proportionate share of the profits of said co-partnership, as hereinbefore specified."

Paragraphs "Sixth" provide that the books of account of the partnerships shall contain a record of

> "all money by them or either of them received, paid out and expended in and about the said business."

Paragraphs "Thirteenth" provide that

> "at the termination of this co-partnership * * * all outstanding book accounts shall be collected at the end of the said co-partnership by them, and all proceeds realized from the collection thereof, less the actual expenses incident to the collection thereof, shall be divided between them * * * "

in accordance with their respective interests.

At the time of decedent's death there were outstanding a large number of accounts for services rendered to patients (R. 22). No entries were made on the partnership books for these services because it was the practice to make no entry until the money had actually been collected (R. 25, 26). The only record of services performed was kept under a card system upon which the time and amount of service performed was recorded (R. 26, 27). Bills were sent out when the case was completed (R. 27). At the time of decedent's death there was no way of determining even the amount of these accounts be-

cause none had been set up on the partnership books (R. 26), and in many instances the services were not completed (R. 22, 23).

At the time of decedent's death there was absolutely no money allocated on the partnership books as his distributive share (R. 20). Petitioners urge that within the meaning of Section 182 there was no net income taxable to decedent as of the date of his death. Certainly there could be no income, either actually or constructively, received by decedent until the partnership had at least constructively received the income. Can it be said that the record of services performed and contained on this card index system by this partnership could on any given date be considered as income constructively received by the partnership? The pertinent provision of the Regulation in that regard is set forth in Article 42-2 of Treasury Reg. 86, which provides as follows:

> "Income not reduced to possession—Income which is credited to the account or set apart for a taxpayer and which may be drawn upon by him at any time is subject to tax for the year during which so credited or set apart, although not then actually reduced to possession. To constitute receipt in such a case the income must be credited or set apart to the taxpayer without any substantial limitation or restriction as to the time or manner of payment or condition upon which payment is to be made, and must be made available to him so that it may be drawn at any time, and its receipt brought within his own control and disposition. * * *"

Decedent's share of the receipts to be collected from the cases then pending and listed on the card index of the partnership could neither be set apart without substantial limitation or restriction, nor be made available to him to be drawn upon by him in 1935.

Article 42-3 of the same Regulation likewise provides for a reference to Section 188 (in Supplement F) of the Act for determining a partner's tax:

> "* * * As to the distributive share of the profits of a partner in a partnership, see Section 188. * * *"

The purpose of the amendment to Section 42 was not to accrue partnership income in computing the tax of an individual partner. Only the income of the decedent need be accrued. An examination of the report of the Ways and Means Committee of the House and of the Finance Committee of the Senate substantiates this position.

The report of the Ways and Means Committee of the House on Sections 42 and 43 (H. Rep. No. 704, 73d Cong., 2d Sess., p. 24) is as follows:

> "Sections 42 and 43. Income accrued and accrued deductions of decedents: The courts have held that income accrued by a decedent on the cash basis prior to his death is not income to the estate, and under the present law, unless such income is taxable to the decedent, it escapes income tax altogether. By the same reasoning, expenses accrued prior to death cannot be deducted by the estate. Section 42 has been drawn to require the inclusion in the income of a decedent of all amounts accrued up to the date of his death regardless of the fact that he may have kept his books on a cash basis. Section 43 has also been changed so that expenses accrued prior to death of decedent may be deducted."

The report of the Finance Committee of the Senate on Sections 42 and 43 (S. Rep. No. 558, 73d Cong., 2d Sess., p. 28) is as follows:

> "Sections 42 and 43: Period for which deductions and credits taken. The courts have held that income accrued prior to the death of a decedent on the cash basis is not income to his estate, and under the present law, unless such income is taxable to the decedent, it escapes income tax altogether. By the same reasoning, expenses accrued prior to death can not be deducted by the estate. Sections 42 and 43 of the House bill were so drawn as to require the inclusion in the income-tax return for the decedent of all items of income and deductions accrued up to the date of death regardless of the fact that the decedent may have kept his books on a cash basis. The change made in Section 43 is necessary to effectuate the policy adopted in the House bill in Section 42. By reason of the proposed change such items as accrued dividends and interest on partially tax-exempt securities are permitted as a credit in computing the normal tax."

In discussing this Section, together with the foregoing Committee reports, the Board of Tax Appeals in the case of *Fehrman v. Commissioner*, 38 B. T. A. 37, concluded that the sole purpose of Congress in enacting said Section was to compute a decedent's income on an accrual basis even though he had theretofore kept his books and made his returns on a cash basis.

The courts have often distinguished between partnership income and the income of the individual partner for tax purposes. It has been held that the Government cannot levy on partnership assets because of a tax claim against the individual partner (*U. S. v. Kaufman*, 267 U. S. 408); a partner cannot offset personal non-capital losses against his distributive share of partnership non-capital gains (*Johnston v. Commissioner*, 86 Fed. (2d) 732); the partners and their partnership can have different fiscal years (*Guaranty Trust Co. v. Commis-*

sioner, 303 U. S. 493), and the partners and their partnership can have different methods of accounting (*Truman v. U. S.*, 4 Fed. Supp. 447; Percival H. Truman, 3 B. T. A. 386; W. J. Burns, 12 B. T. A. 1209; Fritz Hill, 22 B. T. A. 1079).

The Commissioner contends that one of the reasons why his determination of the deficiency should be upheld is that otherwise this particular sum might escape taxation altogether. This is not so, for it is taxable as part of decedent's gross estate. Furthermore, the fallacy of such argument is pointed out in Mertens' "Law of Federal Income Taxation," 1939 Supp., Sec. 4.01, p. 537:

> "It is sometimes urged as a reason for taxability that unless an item is taxed it will escape taxation altogether. This is a question-begging argument if the point to be determined is whether an item is income at all."

As authority the author cites *Commissioner v. Norfolk Southern Railroad Co.*, 63 Fed. (2d) 304, Cert. Den., 290 U. S. 672.

The 16th Amendment, upon which the present income tax is based, authorized a tax on "incomes from whatever source derived." It has been held that either the accrual or the cash method of determining income was permissible. It is extremely doubtful, however, whether such a combination of these methods as the Commissioner seeks to impose upon petitioners under Section 42 accurately determines taxable income within the authorization conferred by the 16th Amendment. As interpreted by the Commissioner, Section 42 would require that taxpayer file a return accounting for all income on a cash basis and superimpose thereon additional items computed on the accrual basis. It is difficult to see how the figure thus arrived at could be held to constitute income within the meaning of the 16th Amendment. The opinion of this Court in *Guaranty Trust*

Co. v. Commissioner, 303 U. S. 493, substantiates petitioners' position in this regard. Mr. Justice Stone therein states:

> "Receipt of income or accrual of the right to receive it within the tax year is the test of taxability, not the time it has taken the taxpayer to earn it, nor the duration of his investments which have finally resulted in profit."

It is to be noted that the Court used the terms "receipt of income" and "accrual of the right to receive it" in the alternative.

Much has been made of the fact that because of decedent's death the partnerships were automatically dissolved, pursuant to the Partnership Law of the State of New York, and that therefore decedent's interest in the partnership accounts became immediately distributable to him. Upon a careful study the fallacy in this argument becomes evident.

The pertinent sentence of Section 42 reads in part that:

> "* * * there shall be included * * * amounts accrued up to the date of his death."

Certainly decedent's share of the partnership accounts could not have accrued up to the date of his death if, as the Commissioner contends, they became distributable upon his death.

In a recent case, *Golden v. Commissioner of Internal Revenue*, 113 Fed. (2d) 590, the Commissioner extended this contention to its logical conclusion and it was there declared untenable by the Court. In that case the decedent was a large stockholder as well as an official of the Golden-Anderson Valve Specialty Co. The company maintained large insurance policies upon its executive officials which were, pursuant to an

agreement, to be distributed when collected directly to the stockholders in proportion to their holdings. Upon the death of Golden this insurance was collected and a large portion paid over to his estate as a stockholder in the company. The Commissioner contended that the proceeds of the policy payable to decedent's estate constituted income accrued to him under Section 42 which should have been reported by the executors in decedent's last return. The Court stated:

> "One minor question remains. Mr. Golden, the insured president of the Valve Company, held, as might be expected, a large portion of its stock. Did his insurance dividend accrue to him individually in the period before his death, or to his estate in the period after his death? The Board's allocation of the dividend to the latter period is, we think, plainly correct. 'All events creating the liability' for that dividend had assuredly not occurred prior to Mr. Golden's death, or even—to split a metaphysical hair—up to and including the moment of his death."

The dissolution of the partnership because of the death of Dr. Wallace can have no bearing upon the taxability of the sum in question as income for the year 1935, as any interest which might accrue to him by reason of such dissolution could not have accrued "up to the date of his death."

POINT II

Assuming that Section 42 applies to petitioners herein, there was no income accrued to decedent as of the date of his death on December 25, 1935.

The partnership agreements specifically provided for an accounting and payment of distributive shares to the partners at

monthly intervals. This was done down to the month of December, 1935. On the date of decedent's death there was no distributive share in the partnership profits on hand due to decedent or to any other partner. True, the partnership had as assets certain accounts for services rendered and certain prospective accounts for medical services rendered for which no fee had then been fixed, but such cannot constitute income in any system of accounting. The fact that in the case of a deceased taxpayer the accrual method of accounting is forced by statute upon the executor of his estate does not mean that the accrual method of accounting is forced upon the partnership of which he was a member.

Several cases decided by the United States Courts indicate most clearly that neither the sum here sought to be taxed as income nor the right to receive it had accrued to decedent at the time of his death in December, 1935. In *Guaranty Trust Co. v. Commissioner*, 303 U. S. 493, this Court stated:

> "Receipt of income or accrual of the right to receive it within the tax year is the test of taxability, not the time it has taken the taxpayer to earn it, nor the duration of his investments which have finally resulted in profit. *Lucas v. Alexander*, 279 U. S. 573.
>
> The Revenue Acts have consistently adhered to that policy in taxing the income of a partner. Since the partner is entitled to profits only upon a partnership accounting at the end of the accounting period, his profits become subject to income tax when and as they are thus ascertained."

Unless the income was actually received by decedent before his death, or his right to receive it pursuant to the terms of the partnership agreements had accrued to him at that time, under

the rule in the case of *Guaranty Trust Co. v. Commissioner*, 303 U. S. 493, it was not taxable income during that tax year. The Commissioner makes no contention that decedent received this income during 1935. Neither was he entitled to receive it. The Commissioner, however, contends that regardless of these considerations, under Section 42, it became "taxable accrued income" upon the day of decedent's death.

The sum herein involved never came into decedent's possession. At no time could he have used the proceeds of the partnership accounts. All the money realized therefrom might conceivably have been paid out for equipment or for other partnership expenses. No part of the partnership funds was decedent's until at one of the monthly accountings the partners divided among themselves whatever part of the cash on hand remained over and above the authorized expenses. Until that division had been made no income could accrue to any of the individual partners.

Many Courts have held many times that income "accrues" only when it is credited to the taxpayer and becomes subject to his disposal without restriction. The Court so stated in *Simms Oil Co. v. Commissioner*, 74 Fed. (2d) 561:

> "Article 51 of Reg. 69, promulgated under the Revenue Act of 1926, followed the well settled principle that income accrues only if it is credited to the taxpayer and becomes subject to his disposal without restriction."

The Commissioner, in construing decedent's share of the accounts receivable of the partnership to be income taxable to decedent as of the date of his death, based such determination, not on facts ascertainable at the time of death, but upon the facts determined between the time of decedent's death and the assessment of the deficiency. The Commissioner, in assessing the deficiency, adopted as the basis for the assessment the ap-

proximate receipts of the estate for the subsequent year (1936). This very fact serves to show the impossibility of determining accurately the value of accounts receivable at the time of decedent's death. Such determinability is a primary test of accruability.

In *Helvering v. Russian Finance & Construction Corp.*, 77 Fed. (2d) 324, the Court in discussing the accruability of deductions, stated:

> "In order to be accruable in the taxable year for which the return is made, a valid obligation to pay must have existed in that year, which is enforceable on the date when the obligation is due. When, however, the obligation to pay is contingent upon the happening of some future event, there is no certainty that it will be paid or will accrue. In such event, no obligation accrued from the fixed or determinable source and no duty arises or exists in the taxable year which can be accounted for as income under any system of accounting."

After studying the problem of accrual of income and discussing thoroughly the various definitions of the word accrue, the Ninth Circuit Court in *H. Liebes & Co. v. Commissioner*, 90 Fed. (2d) 932, concludes:

> "The complete definition would therefore seem to be that income accrues to the taxpayer when there arises to him a fixed or unconditional right to receive it if there is a reasonable expectancy that the right will be converted into money or its equivalent."

Decedent had no fixed or unconditional right to receive the sum in question; even the partnership did not receive it until the year 1936. At the time of decedent's death in 1935 many contingencies intervened before the monies were to be received by the partnership and after it had been received by the part-

nership much still remained to be done before any could be allocated to decedent or his estate as part of his distributive share. These items therefore cannot meet the definition of accrued income as construed in the cases herein cited.

In *Commissioner v. Edwards Drilling Co.*, 95 Fed. (2d) 719, the Court in the Fifth Circuit stated in this regard:

> "It is, of course, true as the Board points out that under the accrual method of accounting employed by petitioner, items must be accrued as income when the events occurred to fix the amount due and determine liability to pay. *United States v. Anderson*, 269 U. S. 422, 46 S. Ct. 131, 70 L. Ed. 347. Generally speaking, however, the income tax law is concerned, and its administration should deal only, with realized losses and realized gains. *Lucas v. American Code Co.*, 280 U. S. 445, 50 S. Ct. 202; 74 L. Ed. 538, 67 A. L. R. 1010. The taxpayer therefore is under no obligation to pay a tax on income he might never receive. *North American Oil Consolidated v. Burnet*, 286 U. S. 417, 52 S. Ct. 613, 76 L. Ed. 1197. A strained construction in administrative efforts to accrue income should be avoided."

Petitioners' position is further supported by the decision of the Board of Tax Appeals in *Fehrman v. Commissioner*, 38 B.T.A. 37. There, the petitioner's decedent, reporting on a cash basis, received from his employer in addition to his salary a certain percentage of the net profits of the store as disclosed by inventory at the end of the calendar year. Decedent died August 14, 1934. His employer ascertained the percentage of profit due to decedent and paid the same to his estate January 1, 1935. In holding that the sum thus paid did not accrue to decedent during the period ending on the date of his death and

was not properly includible in his gross income for that period, the Board stated:

> "It is obvious from the language of the Act and the Legislative intent as disclosed by the Committee reports quoted above, that the purpose of Congress was to treat the income of a decedent as though he were on an accrual basis even though he was actually on a cash basis and kept his books on a cash basis, and that the phrase 'amounts accrued up to the date of his death' means those amounts which would be properly included in a decedent's income if he were on an accrual basis as distinguished from a cash basis.
>
> If petitioner's decedent had been on an accrual basis rather than a cash basis, would the amount paid to the petitioner by the F. W. Woolworth Co. in January, 1935, be properly considered as income accrued to the decedent at the date of his death? It is our opinion that it would not."

The Commissioner claims this case to be distinguishable because of its different factual setup. Petitioners contend, however, that the principles upon which that opinion was based are likewise applicable to the present case. The Board there held that to constitute accrued income to a taxpayer such amounts must be definitely ascertainable at the time as of which the accrual is to be made and the exact amount of compensation be a mere matter of computation. Applying that principle to the present case, it is clear that more than mere computation was necessary in order to determine the sum due decedent from the partnership.

A case analogous to the present is that of *United States v. Wood*, 79 Fed. (2d) 286, Cert. Den., 296 U. S. 643. There decedent was, as in the present case, a member of a partnership.

The partnership continued pursuant to its agreement after decedent's death and at the end of the year decedent's estate was credited with his share in the partnership profits for the portion of the year prior to his death. The Commissioner cited as authority for his position that said income was taxable as of the year of decedent's death, the case of *Darcy v. Commissioner*, 66 Fed. (2d) 581. In distinguishing this case the Court in *U. S. v. Wood*, supra, quoted from the Darcy case and commented thereon thus:

> "The Circuit Court of Appeals said, 'We agree that what is not income in fact cannot be made income by legislative fiat and thus brought within the Income Tax Laws. *Hoeper v. Tax Commission*, 284 U. S. 206, 215; 52 S. Ct. 120; 76 L. Ed. 248. But this actually was decedent's income. For all we know he could have had it as such before he died. He did draw a comparatively small amount between January 1, 1924, and the date of his death. No one can say from this record that he drew all he could.'
>
> In the instant case no partner had the right to demand any part of the profits until the end of the calendar year. In fact, because of the nature of the partnership business the profits could not be determined until that time."

The Court thereupon directed judgment for the taxpayers.

The Circuit Court in the Third Circuit in a companion case to the one at bar, *Enright's Estate v. Commissioner of Internal Revenue*, 112 Fed. (2d) 919, declared that Section 42 did not authorize the assessment of a deficiency in a parallel situation to the present. The Court there stated:

> "In the present case under the partnership agreement as reflected in the partnership accounts and returns, Enright had the right to receive only his proportionate share of the cash receipts of the firm. Of these only $4,143.81 remained distributable to him at his death. We think it is clear from what has been said that this sum represented the partnership income accrued to him up to the date of his death within the meaning of Section 42 of the Revenue Act. In our opinion that section did not require the inclusion as 'amounts accrued' of the uncollected accounts receivable and unbilled fees which under the partnership agreement and its accounting method were not distributable to him."

Petitioners accounted for all income which decedent had received from the partnerships. He was entitled to no more at the date of his death. The deficiency assessed is based upon receipts from the partnership received in 1936 and resulting from winding up its affairs. This, petitioners submit, was error.

A further analogy supporting the holding sought by petitioners is found in the decisions involving the return of income impounded pending the disposal of litigation. *North American Oil Consolidated v. Burnet*, 286 U. S. 414, 423; Trojan Oil Co., 26 B.T.A. 659; National Petroleum & Refining Co., 28 B.T.A. 569. In the North American Oil Consolidated case, supra, this Court held impounded income taxable in the year in which it was actually received. Mr. Justice Brandeis stated:

> "The net profits were not taxable to the company as income of 1936 * * *. There was no constructive receipt of the profits by the company in that year, because at no time during the year was there a right in the company to demand that the Receiver pay over the

> money. Throughout 1916, it was uncertain as to who would be declared entitled to the profits. It was not until 1917, when the District Court entered a final decree vacating the Receivership and dismissing the bill, that the company became entitled to receive the money. Nor is it material for the purposes of this case, whether the company's return was filed on cash receipts and disbursements based on an accrual basis. In neither event was it taxable in 1916 on account of income which it had not yet received and which it might never receive."

The Commissioner submits as authority for his position two recent decisions of this Court: *Bull v. U. S.*, 295 U. S. 247, and *Guaranty Trust Co. v. Commissioner*, 303 U. S. 493. Petitioners have already cited from the opinion in the latter of these two cases as authority for their position. Petitioners submit that neither decision conflicts with their contention herein.

In *Bull v. U. S.*, 295 U. S. 247, no question of accrual was presented. This Court decided that decedent's share of the partnership profits for the portion of the year during which he lived constituted income to him. His share of the profits for the balance of the year was treated as income to his estate. The distinction between that case and the present is clear. The main question in the instant case, whether money received subsequent to decedent's death for work done prior to his death, constitutes income, was not involved. The Court there was concerned solely with profits actually received by the firm prior to and subsequent to the partner's death.

Similarly, in *Guaranty Trust Co. v. Commissioner*, 303 U. S. 493, this Court was concerned only with the taxability of profits received by the firm during the part of the year prior to decedent's death. The question of taxability as income of the

subsequent receipts from accounts for incomplete and unbilled services was not at issue in that case.

On the date of decedent's death the partnership had no assets capable of distribution among the partners in proportion to their respective interests in the partnership. No one could possibly have parceled out the cases indexed on the record cards and say to each partner—"This is your share." The fee to be charged had not been fixed and could only be fixed by the physician in charge of that particular case, not by the partner who might receive that case if such a distribution were attempted. In the event of such distribution one partner might collect one hundred percent on the cases set apart for him, another twenty percent, or perhaps nothing. Such would not be an equitable distribution of partnership assets. In order to effect a proper distribution according to the terms of the partnership agreements it was essential that none of the assets be distributed until they had been liquidated.

POINT III

The decision of the Circuit Court of Appeals for the Second Circuit should be reversed and the deficiency assessed by the Commissioner against petitioners should be set aside.

Respectfully submitted,
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In the Supreme Court of the United States

OCTOBER TERM, 1940

No. 479

NORMAN J. PFAFF AND FRANK B. WALLACE, EXECUTORS OF ESTATE OF WILLIAM L. WALLACE, DEC'D, PETITIONERS

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE RESPONDENT

We do not oppose the granting of the petition for a writ of certiorari in this case.

The question involved is whether his share of income, earned but not yet received by a partnership, should be included in the gross income of a partner for the taxable period ending with his death, where both the partnership and the deceased partner kept books on the cash basis. The court below held that the deceased partner's share of income earned for the taxable period ending with his

death should be included in his gross income for that period. In this respect its decision is in direct conflict with the decision of the United States Circuit Court of Appeals for the Third Circuit in *Estate of Enright* v. *Commissioner*, 112 F. (2d) 919, pending on petition for certiorari, No. 436, October Term, 1940.

The Government has filed a petition for a writ of certiorari in the *Enright* case on the ground that it is in direct conflict with the decision of the Circuit Court of Appeals for the Second Circuit in this case (113 F. (2d) 114).

For the foregoing reason, the issuance of a writ of certiorari in the present case is not opposed.

Respectfully submitted,

FRANCIS BIDDLE,
Solicitor General.

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In the Supreme Court of the United States

OCTOBER TERM, 1940

No. 479

NORMAN J. PFAFF AND FRANK B. WALLACE, EXECUTORS OF THE ESTATE OF WILLIAM L. WALLACE, DECEASED, PETITIONERS

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The memorandum opinion of the Board of Tax Appeals (R. 9–11) is not officially reported. The *per curiam* opinion of the Circuit Court of Appeals (R. 48) is reported in 113 F. (2d) 114.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on July 24, 1940 (R. 48–49). The petition for a writ of certiorari was filed on Octo-

ber 1, 1940, and granted on November 12, 1940 (R. 49). The jurisdiction of this Court rests upon Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether a deceased partner's share of income earned, but not yet received, by the partnership should be included in the gross income of the partner for the taxable period ending with his death, where both the partnership and the partner kept books on the cash basis.

STATUTES AND REGULATIONS INVOLVED

The pertinent statutes and regulations are set forth in the Appendix to our brief filed in *Helvering* v. *Enright,* No. 436, this Term, to be argued herewith.

STATEMENT

The pertinent facts, as found by the Board of Tax Appeals (R. 9–11), may be summarized as follows:

During 1935 the decedent, a practicing physician, was a member of two medical partnerships: one created in 1933 and dissolved by limitation of the partnership agreement on June 30, 1935, and the other created on July 1, 1935, and in existence at the date of his death on December 25 of that year. In each partnership the decedent was entitled to 40 percent of the profits. The second

partnership, upon organization, took over the assets and assumed the liabilities of the prior partnership. (R. 9.)

At the time of decedent's death there were partnership accounts outstanding for services rendered patients during decedent's lifetime in a total amount of $69,061.59, of which decedent's share was 40% or $27,624.64. How much of this total represented accounts receivable of the first partnership is not disclosed. Between the date of decedent's death and October 1, 1936, net payments received on these accounts aggregated $16,251.21, of which $5,961.80 was paid decedent's estate as his net distributive share. On the last named date decedent's interest in the remaining uncollected accounts was sold by his executors for $500. In the estate tax return filed for decedent's estate his interest in these uncollected accounts of the partnership, as of the date of his death, was included at a value of $6,693.14. (R. 9, 11.) Each of the partnerships maintained its accounts on a cash basis (R. 9).

The Commissioner increased decedent's gross income by $5,689.19,[1] as the sum accruable on account of his interest in these partnership receivables at the time of his death, under Section 42 of

[1] The Board noted (R. 10–11) that the Commissioner, "in his determination of the deficiency, has not included in decedent's income, as accrued, his 40 percent share in these accruables, at their face amount. Only approximately 20 per cent of that face value is included."

the Revenue Act of 1934 (R. 6, 9–10). The Board of Tax Appeals upheld the determination of the Commissioner (R. 11). Upon appeal, the Circuit Court of Appeals for the Second Circuit affirmed the decision of the Board *per curiam* (R. 48).

ARGUMENT

This case is identical in all essential respects with *Helvering* v. *Enright,* No. 436, this Term, to be argued herewith. We therefore respectfully refer the Court to the argument in our brief filed in the *Enright* case.

One minor point of difference affects Point 3 (pp. 28–34) of the argument in our brief in the *Enright* case. The taxpayer in the *Enright* case contends that "the earned proportion of the estimated receipts from unfinished business" was not "accrued" within the meaning of Section 42 of the Revenue Act of 1934. No such problem arises here. The outstanding accounts in the instant case would be considered "accrued" under any system of accrual accounting. *Continental Tie & L. Co.* v. *United States,* 286 U. S. 290, 296. Furthermore, there scarcely can be any question as to the valuation placed by the Commissioner upon these outstanding accounts. As the Board noted (R. 11): "The amount included by respondent is less than the amount actually realized from decedent's interest in these receivables and is less than the amount declared by petitioners

as the value of these receivables in the estate tax return which they filed."[2]

CONCLUSION

It is submitted that, for the reasons stated in our brief filed in *Helvering* v. *Enright,* No. 436, this Term, to be argued herewith, the decision of the court below is correct and should be affirmed.

Respectfully,

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FEBRUARY 1941.

[2] See also note 1, *supra*, p. 3.

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SUPREME COURT OF THE UNITED STATES.

No. 479.—October Term, 1940.

Norman J. Pfaff and Frank B. Wallace, Executors of the Estate of William L. Wallace, Deceased, Petitioners, *vs.* Commissioner of Internal Revenue.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[March 31, 1941.]

Mr. Justice Reed delivered the opinion of the Court.

This case presents the same question as *Helvering* v. *Enright*, decided today. Petitioners are the executors of a deceased physician who during 1935 was a member of a medical partnership and entitled to forty per cent of its profits. He died December 25, 1935, on which date there were outstanding about $69,000 of partnership accounts receivable for services rendered to patients during his lifetime. His death worked a dissolution of the partnership under § 62(4) of the New York Partnership Law. The decedent's interest in these accounts came to over $27,000. Both he and the partnership were on a cash basis. Pursuant to section 42 of the Revenue Act of 1934 and article 42(1) of Treasury Regulations 86, the commissioner included the decedent's share of the accounts receivable in his 1935 income, though only at about one-fifth of face value. The Board of Tax Appeals sustained the commissioner's view of the statute, and also ruled that the valuation of the decedent's interest in the accounts at one-fifth of face value was amply supported. The Circuit Court of Appeals, without writing an opinion, affirmed the Board. 113 F. (2d) 114. Because of a conflict with the Third Circuit's decision in the *Enright* case, *supra*, we granted certiorari.

There is no relevant difference between these facts and *Helvering* v. *Enright*. For the reasons stated in that opinion it was proper to include in the decedent's 1935 income the fair value of his interest in the accounts.

Affirmed.